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***Using Performance Budgeting to Improve Service Delivery: A Case Study  
of the Mpumalanga Department of Health.***

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**A [minor]dissertation submitted in [partial] fulfilment of the  
requirements for the award of the degree of Master of Philosophy in  
Public Policy.**

**Faculty of the Humanities  
University of Cape Town  
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**COMPULSORY DECLARATION**

**This work has not been previously submitted in whole, or in part, for the  
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## ACRONYMS

ANC	African National Congress
ASGISA	Accelerated and Shared Growth Initiative for SA
FFC	Financial Fiscal Commission
IGFRA	Intergovernmental Fiscal Relations Act
IFR	Intergovernmental Fiscal Relations
MTEDF	Medium-term Expenditure Delivery Framework
MTBPS	Medium Term Budget Policy Statement
MTEF	Medium Term Expenditure Framework
OECD	Organisation of Economic Countries Development
PBF	Performance Budgeting Framework
PFMA	Public Finance Management Act
PPBS	Planning-Programming Budgeting System
SALGA	South African Local Government Association
SMS	Senior Management System
TBBS	Target-Based Budgeting System
UK	United Kingdom

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## **ABSTRACT**

Public policy is a tool through which government can successfully deliver services to its people. In a transforming country like South Africa, it is difficult to deliver services to the majority of people due to the previous apartheid political structures, systems and dispensation that denied the majority of black South Africa citizens in particular, their basic rights, including their rights in respect of health care.

Thus, the most significant challenge facing the South African health system under the new democratic dispensation is to provide equitable health care services to all in the country. This can be achieved through an equitable distribution of resources between the public and private health care sectors, urban and rural areas and across and within provinces. Budgeting is an important tool which can be used to achieve policy objectives and improve service delivery. This thesis evaluates implementation of budget reform within the Department of Health and Social Services in Mpumalanga, and the extent to which this has led to implementation of policy objectives and improved equitable service delivery.

Chapter 1 sets out the rationale for the study and looks at the research design and methodology applied.

Chapter 2 reviews budget reform in the Organisation of Economic Countries Development (OECD). This chapter focuses on the theoretical review of performance budgeting systems, detailing its various components including strategic planning and financial planning. It also looks at the limitations of traditional budgeting in terms of resource allocations.

Chapter 3 reflects a theoretical review of budget reform in South Africa. It focuses on the country's legal framework for budgeting as well as the linkages between policy priorities and budgetary allocations.

Chapter 4 describes implementation of performance budgeting systems in the Mpumalanga Department of Health and Social Services. It describes how performance budgeting systems improve service delivery.

Chapter 5 recommends the following for successful implementation of performance budgeting systems:

- Importance of linking policy priorities with budgetary allocations;
- Improvement of capacity at managerial level; and
- Educating politicians about performance budgeting systems.

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## **CHAPTER 1**

### **1. Introduction**

One of the most difficult tasks of budgetary management is ensuring that the budget adequately reflects government policies and priorities.

Traditionally budgets focused on an incremental input approach. This resulted in a lack of clarity regarding resource allocation and the growth of bureaucracies (McGill, 2001). In traditional “line item” budgeting, budgets appropriate funds to agencies against detailed input categories, and agencies were largely unable to shift funding from one line-item to another. In other words, “line-item” budgetary allocations were not based on outcomes/outputs which resulted in confusion and duplication of functions.

Thus, from the 1960’s there has been a global surge towards budget reform. The last few decades has seen many governments attempting to establish a results oriented budgeting approach. Results-oriented or Performance-Based Budgeting (PBB) has been gradually adopted as a key public sector reform initiative in developing and developed countries such as the United States, Australia and New Zealand. Global support for budget reform is based on the need for efficient resource allocation by governments.

This is evident in the South African case as well. In a society undergoing political and economic transformation, the imperative for public service delivery to redress past imbalances is essential. South African economic relations are characterized by a market-based system of ownership of capital and distribution of wealth and income. The permutations in the economic system have historically been defined by race (PCAS, 2006). Prior to the attainment of democracy in 1994, South Africa was a country marked by extreme inequalities with, for example, the health policies being instrumental in maintaining economic and political power for the white population group.

The differences in the health status and allocation of health resources reflected the excessive inequalities between black and white population groups, urban and rural communities, the rich and the poor (Chetty, 2007: 1). The health system was fragmented between fourteen different Departments of Health, comprising of the ten 'home lands' departments, three 'own affairs' departments, and one 'general' affairs department. Chetty (2007) argues that this fragmentation of departments resulted in a system which was not cost effective, lacked coordination, decreased access and provided differential quality of care for the different population groups.

The most important feature of the apartheid era was the racial segregation of the health facilities. There are reports of overcrowded and understaffed black hospitals. Chetty (2007) argues that the former 'homeland', 'township' and informal settlements were systematically under funded as a result of apartheid policy. The apartheid government specialized on use of private health care which excluded the majority of the black population. The private sector health facilities were mainly accessible to the white population group and a minority of black people who could afford it (Chetty, 2007: 2). For example, in 1992/93 expenditure in the private sector health facilities, which cared only for approximately 23% of the total population, was estimated to be 61% of total health expenditure. But post 1994 policies have resulted in tremendous shifts in terms of health allocations to different racial groups.

In 1994 the African National Congress (ANC) won an overwhelming victory in South Africa's first democratic elections and became the ruling party in government. It has maintained its position as the ruling party in government since 1994.

In preparing to govern, the ANC developed a National Health Plan that essentially formed the basis of the democratic government's health policy and included proposals on changes to the governance (i.e, structures, systems, processes, etc) and delivery of health services to all in the country. The ANC's National Health Plan was one of the first comprehensive plans for post apartheid South Africa which firmly entrenched the principles of social justice and equity in respect of health services (ANC, 1994). The vision of the National Health Plan clearly states that 'the health of all South Africans will be secured and improved mainly through

the achievement of equitable social and economic development. This refers to the level of employment, the standards of education, and the provision of housing, clean water, sanitation and electricity.” (ANC, 1994).

The new democratic government, using the ANC’s National Health Plan and its Reconstruction and Development Programme, drafted a White Paper for the transformation of the National Health System in South Africa. The White Paper mapped out the future direction and programme of action for the transformation of the health sector in South Africa and was used as a basis for the drafting of The National Health Act No. 61 of 2003.

Both the White Paper and National Health Act of 2003 play a crucial role in resource allocation to and within the health sector. Chetty (2007) argues that one of the greatest challenges facing the democratic government in 1994 was addressing the inequities in public sector financing. In 1994/95, the National Department of Health introduced a resource allocation formula, aimed at addressing the massive inequities that existed between provinces in terms of public health care spending. With the adoption of the new constitution of the country in 1996, significant autonomy and powers were given to provinces; including powers to Provincial Legislatures to determine functional/sectoral budgets for their respective provinces. A new budgeting system was introduced, whereby National Treasury determined the divisions of revenue between the country’s three spheres of government, i.e., national provincial and local government. The formula works as follows:

- Vertical Split – the division of revenue in respect of concurrent national and provincial legislative competence. The vertical split includes conditional grants for certain programmes, which flow from national departments to provinces;
- Horizontal Split – division of revenue for exclusive provincial legislative competence, between provinces and recently also division for local government functions. This allocation is called equitable share and is an unconditional allocation of revenue to each province to provide all provincial functions.

Despite this new budgeting system, the most significant challenge that continues to face the South African health system is to provide an equitable distribution of resources between the public and private health care sectors, urban and rural areas and across and within provinces relative to the population served by each (Chetty, 2007: 20). It is important to note that the legacy of apartheid policies in South Africa, are persistently large disparities between racial groups in terms of socio-economic status, occupation, education, housing and health.

Linking policy objectives and resources is essential. Policy objectives must take into account the availability of resources and the objectives must be measurable so that they can be monitored and evaluated. This thesis intends to explore whether the budget system in South Africa reflects the policy priorities of the government of the day. The current policy priorities of the South African government are based on the following categories of the economy:

- Macroeconomic Issues
- Infrastructure Investment
- Education and Skills Development
- Industrial and Sector Strategies
- Second Economy Initiatives
- Governance and State Capacity Issues

(ASGISA, 2006)

In the past most budgets in South Africa were structured along departmental lines and not along programmatic lines. It was difficult to establish direct linkages between policy objectives and the funding needed to deliver services in support of those objectives. One of the first attempts at reforming the budgetary system in South Africa has been the adoption of performance budgeting by provincial departments; a move necessitated by the need to align provincial programs with national programs and to comply with current legislation such as the Public Finance Management Act (PFMA). Lack of compliance and failure to align programmes could result in heavy penalties for provinces. Mpumalanga Province was one of the first provinces to adopt and implement a performance budgeting system. It is the first time that such a system has been initiated at a provincial level.

Robinson and Brumby (2005) define performance budgeting as procedures or mechanisms intended to strengthen links between the funds provided to public sector entities and their outcomes and/or outputs, through the use of formal performance information, in resource allocation decision-making. The core objectives of performance budgeting are enhanced allocative and productive efficiency in public sector expenditure. In respect of allocative efficiency, performance budgeting reformers believe that expenditure allocation in the public sector tends to be insufficiently responsive to changing social needs and priorities (Robinson & Brumby, 2005: 13). Performance budgeting is seen as the solution to the inefficiencies in resource allocation in the public sector.

Robinson and Brumby (2005) further define performance budgeting as a system of budgeting which integrates the processes of strategic planning, financial planning and financial management, with an emphasis on performance so as to improve allocative efficiency and delivery efficiency. It is a budgeting technique which focuses on delivery oriented resource allocation and financial planning. The Chief Directorate: Health and Social Services in Mpumalanga has begun restructuring towards a more decentralized, district-based system, in recognition of the need to improve service delivery at local / community level. In this thesis I will assess the implementation and impact, in terms of service delivery, of the performance budgeting system within the Department of Health and Social Services in Mpumalanga.

Since the advent of democracy in 1994, the South African Government has introduced a wide range of reforms aimed at addressing historical imbalances and ensuring fair distribution of resources. Khalo and Fourie (2006) argue that some of the reforms relate to the effective management of public funds, in particular budget reforms. The transformation of public financial management in South Africa is based on key elements such as transparency, accountability and the integration of policies that would lead to a comprehensive budgeting system aimed at accelerating service delivery ( Khalo & Fourie, 2006: 131). These are the important principles for good governance. Good governance dictates that government operations and decisions should be made openly and with the active participation

of those people influenced by them. The budget is the primary economic policy instrument of the government, thus transparency and participation in the budget are particularly important (Folscher, Krafchik & Shapiro, 2000: 8).

Budget transparency and accountability is encouraged at the provincial level through each province preparing its own budget. These are submitted, to each respective Provincial Legislatures as Expenditure Estimates, supported by a Budget Speech and, in most provinces, Budget Reviews. Another document, the Intergovernmental Fiscal Review, is published later in the year and adds sectoral contextual information on provincial expenditures. A pre-budget statement, the Medium Term Budget Policy Statement (MTBPS), was issued for the first time by government in 1997. This package of documents brings South African practice in line with the best practice fiscal transparency measures for fiscal reports posed by the OECD countries (Folscher, 2000: 23). Until the enactment of the PFMA, fiscal reporting to the Legislatures took place once a year and Audited Financial Statements were available two years after the budget had been adopted. Both the frequency and timing of fiscal reporting made it difficult for Legislatures to fulfill their oversight role.

However, in accordance with the PFMA, audited statements on spending by provincial and national departments, legislatures and enterprises must be presented to the Legislatures within seven months, after the end of the fiscal year. This is five months earlier than was previously the case in that under the old system audited statements were usually only presented a year after the end of the fiscal year. Folscher (2000) stipulates that a more significant change is the requirement that the National Treasury must also publish monthly statements within 30 days after the end of each year on actual revenues and expenditure per vote. In areas such as the availability of information, progress has been remarkable.

Globally, budget reform can be traced back to the early 1900's when new budgeting systems were introduced by various governments to replace the traditional budgeting system which focused on expenditure controls. The aim of the traditional budget process was simply to keep control over all money spent by government (Abedian and Strachan, 1998: 54). Budgets were initially viewed as



technical tools with a strong focus on expenditure control and accountability, rather than on deliverables and creating appropriate incentives (Khalo & Fourie, 2006: 132).

In traditional budgets, all expenditures were listed by line item, which means that budgets showed exactly how much had been spent on each type of expenditure. However, it was a good budget system in that it focused on input expenditure such as salaries and wages with no output and outcome information. In the South African context, output and outcome information is necessary because the current legislation such as the Public Finance Management Act (PFMA) and National Treasury Regulations emphasize openness in the budget process. Openness and accountability in the budget process will minimize the misappropriation of funds by government officials. It also enables oversight institutions like the Auditor General and the Financial Fiscal Commission (FFC) to monitor whether budgets are allocated according to the policy priorities of government.

After 1994, there was a need to reform general government administration which included changes in the approach to budgeting. The goal of many government departments in South Africa is to reprioritize and restructure in order to render a more efficient and effective service to the public, given various constraints on the budget and the allocation of the funds. To make service delivery possible it is important to consider Performance Based Budgeting and in ways in which it can be implemented in the South African context. During the apartheid era South Africa was characterised by high economic inequality and levels of poverty. Since 1994, there has been further deepening of inequality and poverty. According to Adato, Carter and May (2006) this inequality represents a deeper and more systematic component of the South African social and economic reality.

### **1.1 Research Problem**

Improving the quality of public service delivery has been a consistent theme of the South African government's policy framework in the transformation of its public service institutions since 1994. Since the attainment of democracy, the State has been successful in achieving macroeconomic stability. Income poverty alleviation

by the State has mainly been through the system of social grants, with both government expenditure and the number of beneficiaries having increased more than three fold since 1994. Changes in the taxation structure have also improved disposable income. Human capital poverty alleviation has taken the form of programmes in the areas of education, health, water sanitation and electricity (PCAS, 2006: 9). These have quantitatively and qualitatively improved the lives of millions in South Africa. Asset capital poverty alleviation, through the housing and land programmes, has seen massive resources transferred to individuals and communities.

However, the legacy of apartheid as mentioned above remains huge, with millions still unable to access basic necessities as clean potable water, electricity and shelter. In order to enhance the delivery process it is essential to have a budgeting system in place which encourages efficiency, accountability and transparency in the public sector. South Africans have experienced frustration with performance gaps in government, particularly at the local level where vital municipal services are delivered. Efficient public administration is essential for translating budgets into effective public services that contribute to positive social and economic outcomes. The government of South Africa is working to enhance performance management at all levels.

One of the factors that negatively affect service delivery in South Africa is the manner in which funds are managed by government. Other factors are lack of human resource capacity and corruption and difficulties experienced in allocating scarce resources. Budgets are the key instrument for translating national priorities into actions and a key instrument for domestic accountability as its implementation is subject to scrutiny by the legislature and external audits (Third International Roundtable, 2007).

It is stipulated in the (OECD) Journal on Budgeting that a government cannot perform if its budget does not. Regardless of a government's determination to orient management and service delivery to results, if budget allocations disregard performance, politicians and managers will too (Schick, 2003: 199). However, applying the budget as an instrument of performance has proven exceedingly

difficult to implement. Performance budgeting critics like Schick argue that performance does not necessarily result in good budgeting. Schick (2003) argues that the problem is not in how we measure performance but in how we use the results. He argues that performance information can affect behaviour only if it is used, and if it is used only when there are opportunities and incentives to do so. According to Schick, one of the reasons that contribute to the failure of budgeting systems is the assumption that budgeting drives management. If the budget is oriented to performance, managers will drive their organizations to perform. Schick (2003) argues that this reasoning led governments to single out budgeting for reform without reforming other managerial behaviour or incentives.

Schick (2003) further argues that this approach is flawed in that it fails to recognize that budgeting is shaped by the managerial context within which resources are allocated and services provided. If the managerial conditions discourage attention to results, efforts to introduce performance budgeting will fail. Budgeting cannot be reformed in isolation of the managerial systems and practices in which it is embedded. I support Schick's view and believe that this flaw could result in the failure of performance budgeting in South Africa, in that currently South Africa focuses its resource allocation more on the system of performance budgeting without addressing necessary improvements at managerial levels. Only if government entities are managed on the basis of results will they be able to allocate resources on this basis.

## **1.2 Research Question**

This thesis aims to answer the following research question: To what extent does a performance budgeting system facilitate service delivery within government departments in South Africa?

Some subsets of questions that the research answers are:

- How does government define performance?
- What are the different formal approaches to assessing and improving performance?

- Why is performance budgeting important for government departments?
- How can accountability be improved when applying performance budgeting?
- Has performance budgeting begun to improve service delivery within the Department of Health in Mpumalanga?
- Why is it important to link performance budgeting with policy priorities of government?
- Who is responsible for implementing performance-based budgeting and specifically, for operationalising measures?
- What oversight capacity, in respect of performance budgeting, is provided by the legislature in South Africa?

### **1.3 Hypothesis**

The main hypothesis is that provincial government departments are using performance budgeting as a tool to improve service delivery. Another hypothesis is that service delivery is influenced by the link between policy priorities and performance budgeting. There is also an assumption that provincial public servants are directly involved in the performance budgeting process. The current legislature is providing an oversight capacity in ensuring that performance budgeting is used as a tool to improve service delivery. In order to realize the impact of performance budgeting there is a need for accountability to take place at both national and provincial level.

### **1.4 Methodology and Research Design**

This is a qualitative research study using a case study approach and interviews with a purposive sample of government officials from the Mpumalanga Department of Health. Documentary analysis and literature reviews were undertaken on performance budgeting, information audits, government reports and budget documents, OECD journals on budgeting and internet searches on the topic. A literature review of current thinking and practice with regard to performance budgeting implementation and reporting is part of the study. This focused on the

approaches adopted by international organizations as well as in selected OECD countries. The thesis is based on a qualitative data analysis.

According to Babbie and Mouton (2001: 270), the primary goal of studies using this approach is defined as describing and understanding rather than explaining human behaviour. In compiling this research, three senior government officials from the Department of Health and Social Services in Mpumalanga were interviewed. The purpose of interviewing these officials was based on the idea that they are directly involved in the budgeting process and they have the knowledge and history of budgeting within the department. The three officials interviewed are Chief Director of Hospital Services, Acting Chief Financial Officer and Director of Financial Accounting and Director of Pharmaceuticals. Both note taking and tape recording were used to collect data during interviews. Tape recording and notes were transcribed. The interviews were unstructured and this has helped in terms of getting the sense of how these officials understand the link between performance budgeting and service delivery. Mpumalanga Department of Health and Social Services was chosen as the case study for this thesis because the Department was characterized by budget discrepancies and therefore provides a good example of how performance budgeting can be implemented in such difficult conditions.

The thesis compares current efforts to undertake budget reform in OECD countries. International comparative research in OECD countries of Australia, Canada, Sweden, the Netherlands, United Kingdom, Denmark, United States, and New Zealand to illustrate some of the main principles in budget processes. These countries are the front-runners of performance budgeting. Information was gathered from several sources. Programme Managers from Mpumalanga Department of Health and Social Services specializing in this field were selected and interviewed. The discussion on performance budgeting in the Mpumalanga Department of Health and Social Services is compared to the experiences of the OECD countries.

When examining performance budgeting, the following key areas were the focus:

- performance management;

- performance measures;
- the budget decision-making process; and
- a legal framework for budgeting

It is extremely difficult to obtain an accurate picture of the state of performance budgeting in South Africa because government departments are still in the initial phases of implementation of the process.

### **1.5 Limitations**

The case study used and the numbers of civil servants interviewed limit the study. The numbers interviewed are too small for the findings to be used to make definitive or generalized conclusions. The other limitation is based on the study being conducted at provincial level only. As such it does not include data for district and sub-district level managers who might have different perceptions of performance budgeting and its effect to service delivery.

### **1.6 Chapter Summary**

Chapter 1 focused on the background of budget reform in OECD countries and in South Africa. The last decades has seen many governments attempting to establish a result oriented budgeting approach mainly due to the failure of previous traditional budgeting methods. Such traditional budgeting methods were based on line-item budgeting which was mainly focused on inputs instead of outputs and outcomes. As a result many OECD countries opted for results-oriented budgeting systems. Results oriented or performance based budgeting systems has been gradually adopted as a key public reform initiative in developing and developed countries. However, implementing budgeting as an instrument of performance has proven to be a difficult task. In this chapter, the importance of managerial behaviour was highlighted as a crucial factor in fostering good performance budgeting systems.

Schick (2003) pointed out that the reasons why many budget reforms failed are that they ignored managerial behaviour or incentives. He argues that this was flawed,

for it failed to recognize that budgeting is shaped by the managerial context within which resources are allocated and services provided. South Africa is identified as one of the victims of this flawed budgeting system. In the past, prior to 1994, budgets in South Africa were structured along departmental lines and not programmatic lines. It was difficult to establish direct linkages between policy objectives and funding needed to deliver services in support of those objectives.

The next chapter examines the evolution of budget reform in more detail.

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## **CHAPTER 2**

### **2. Overview of Budget Reform**

#### **Introduction**

This thesis assesses the role of performance budgeting as a tool that can facilitate service delivery of government departments in South Africa. Budget reform is a recent initiative in South Africa and it is evident that many government departments are still struggling to implement it properly. Services can only be delivered if the means and capacity to do so exist. Since the budget is the primary tool available to governments to effect redistribution and delivery, it is inevitable that reforms of government must include changes to the budget system (Walker & Mengistu, 1999: 10).

In the past decades, there has been a fundamental restructuring of the budget management systems in OECD countries. Lack of data on the costs of particular services made it exceedingly difficult to link resources and results. This is one of the factors that prompted the restructuring of the budget management systems in OECD countries. Diamond (2001) argues that the previous approach to budget management focused on resource allocation and input control, and was usually highly centralized. A highly centralized system of budgeting will not work in South Africa because current legislation such as the PFMA is against such budget centralization. The PFMA is based on transparency and accountability which makes it undesirable for departments to centralise their budgets.

It is said that central budgeting agencies focused on control and compliance as the primary modus in budget management (Diamond, 2001: 3). Diamond (2001) further argues that there was little follow-up in examining the subsequent performance of spending departments. It is for this reason that OECD countries like Australia and New Zealand opted for budget reform initiatives. Diamond argues that OECD countries have opted for medium term budget planning, where fiscal targets are set on a three-to-five year basis rather than on a traditional one-year basis. Australia has taken the approach further than most OECD countries by



developing a forward estimate system, where refined forward estimates become the estimates of the spending rather than simply forecasts of existing policies (Diamond, 2001: 12). Within OECD countries there has been an increasing reorientation of central budget offices away from compliance issues based on detailed control of inputs, to more performance oriented managerial issues that are concerned with outputs and outcomes. OECD countries have opted for budget reform because traditional budget systems, based on short-term and detailed control of inputs, have generally been discredited as a tool for promoting public sector performance which, by definition, should focus on the outputs or the impact resulting from these inputs. Thus many OECD countries have shifted their focus to performance budgeting.

Performance budgeting refers generally to the process of linking expected results to budget levels but not to any particular approach (MacGill, 2001: 377). Improving and measuring performance has pre-occupied governments for at least half a century. Over the past two decades, public sector performance has taken on special urgency as OECD countries have faced recession and mounting demands for more and better public service (OECD, 2004:2). According to an OECD policy brief (2004), performance or results-based budgeting, management and reporting is the latest trend in attempts to improve government performance. These reforms seek to refocus management and budgeting processes away from inputs towards results.

Performance budgeting was first recommended by the Hoover Commission in the US in 1949 (OECD Policy Brief, 2004). The Hoover Commission's "performance budget" was intended to shift the focus away from inputs of government to its functions, activities, costs and accomplishments. Thus rather than emphasizing items of expenditure such as salaries, rent and supplies, performance budgets were to describe the expected outputs resulting from a specific function or activity, e.g. weapons or training (MacGill, 2001: 377). This shift from inputs to outputs was based on the fact that, in the 1940's, OECD countries were struggling to allocate resources in an optimal manner. The budget allocation of these countries was only on inputs without taking into consideration the outputs and outcomes of such inputs. Budgeting was done separately from policy. These countries could not implement their policy priorities and there was no connection at all between their

budgets and their policy priorities. In the 1950s and 1960s many OECD countries, including the USA, started using performance indicators and targets to assess agencies, not on how much they spent, but on what they actually produced. Australia and New Zealand were the first countries to begin the present round of performance management and budgeting in the late 1980s. They were followed in the early to mid 1990s-by Canada, Finland and Denmark (OECD, 2004, 4).

An OECD policy brief (2004) stipulates that governments have introduced performance based budgeting for four main reasons: (1) to improve efficiency in decision-making in budget processes; (2) to promote transparency, (3) to promote accountability; and (4) to achieve savings. This was necessary because decision-makers were not open enough about where money was being spent which also created fragmentation and inefficiency in terms of resource allocation. It is important to note that this is not only with regard to the financial issue but also applies to the management issue. For performance budgeting to work, it is important to sort out both performance and managerial issues. In the past the focus was only on the performance issues and this is the reason why past budget reforms failed.

MacGill (2001) argued that despite recorded successes, concerns remained that the budget did not adequately link “programs with their costs”. Moreover, classical scholars like, Aaron Wildavsky have questioned the traditional type of budgets. For instance they argue that the typical line item budget does not match with the set programmes of government and that they only focus on inputs and not outputs and have a fragmented focus on budget changes (Khato & Fourie, 2006: 132). It is crucial to note that budgeting has to be linked with government policy priorities and planning. Government’s policy priorities and plans are translated into action through strategic planning. Policy priorities must be linked to the budget. There is no point in having policy priorities if there is no budget to implement them. Thus it is important to plan these together. In the past these were done separately.

## **2.1 Why the Need for Budget Reform in OECD Countries?**

Reasons that led to budget reform by OECD countries include increase in oil shocks, low growth and inflation, rising unemployment and escalating fiscal deficit. Schick (2001) argued that this led to government expansion (Schick, 2001: 4). He further argues his point by providing statistics that show that rapid government expansion led to budget reform in these countries. Schick (2001) stipulates that in 1960, the OECD's first year, total government outlays of OECD countries averaged 29 percent of GDP. Two decades later, these outlays averaged 40 percent of GDP, an increase of more than one half percent point a year. Most of the growth was in social security transfers which doubled from 7 percent of GDP to 14 percent of GDP.

Schick (2001) emphasized that the huge expansion of government was promoted by governments which reengineered their budget practices to boost spending. When economic conditions deteriorated in the 1970s, public budgets were still on an expansionary course. There was an unsustainable imbalance between the momentum of the budget and the capacity of governments to maintain a prudent fiscal course (Schick, 2001: 7). Many governments wanted to limit their public spending by improving fiscal targets in advance of the annual budget preparation cycle. Schick (2001) stipulated that the early targets were set independently of the budget process without careful consideration of revenue capacity or of the steps needed to implement them. South Africa also managed to cut budget deficits even though social inequalities and poverty was extremely high.

Moreover, Schick (2001) argued that many countries set targets at unrealistic levels and that the targets had to be deserted far short of their stated goal. On the other hand, he argued, that the second generation targets that emerged in the 1980s and the early 1990s have been somewhat more effective to the extent they are linked to budget decisions and are enforced through procedural constraints on government action. Schick (2001) further argued that the most important recent innovations have included fiscal targets covered in the medium-term expenditure frameworks, targets imposed by international treaties or organizations, accrual accounting and budgeting, baseline projections used to estimate budget impacts of current actions

and codes of fiscal responsibility that require transparency in government fiscal policy (Schick, 2001: 7). In the 1980s, the OECD countries realized the importance of incorporating strategic planning processes with budgeting processes.

Schick (2001) highlighted in his paper that the long-standing tendency in budgeting has been for government to be explicit about its priorities and to have priorities imputed from the allocations actually made rather than to state them in advance. If government does not know its priorities, the budget will not reflect them. Schick (2001) noted that strategic planning has emerged in recent times as the main innovation in enabling government to structure its budget on the basis of missions and objectives (Schick, 2001: 15). It is for this reason that in the 1980s, Australia, New Zealand and Sweden decided to improve performance in budgeting process. Each of these countries moved boldly to shift budgeting from compliance to performance by giving managers freedom to run their operations as they deemed appropriate (Schick, 2001: 22).

Moreover, most OECD countries realized that the line-item approach of budgeting had several impediments to promoting effective public planning and management and to fostering results-oriented accountability in public sector institutions (Shah and Shen, 2007: 139). According to Shah (2007) a line-item budget emphasizes inputs, it provides information on how much money is spent and how it is spent rather than on what it is spent. He further argues that line-item budget does not link inputs with outputs and therefore says nothing about how efficiently resources are used.

During the time of line-item budgeting, managers were not given any managerial discretion. As a result Shah and Shen (2007) argue that line-item control leads to micromanagement of agency operations by central budget offices and finance ministries and to hierarchical controls within the agency. The OECD countries introduced budget reforms as a mechanism for dealing with these inefficiencies, The set of reforms initiated in the 1950s linked planning with budgeting through program budgeting. In the 1960s, the reform initiative focused on aggregate sectoral allocations through block-vote budgeting. This form of budgeting refers to line agencies being given larger appropriations with the powers of discretion to

move funds across spending categories without seeking central approval (Shah and Shen, 2007: 139). These budget reform approaches led to the experimentation of zero-based budgeting in OECD countries. Shah and Shen (2007) describe zero-based budgeting as the budgeting approach whereby every item of expenditure had to be justified again every year, so that funds were allocated to meet current policy priorities.

However, zero-based budgeting was quickly abandoned when the technique proved impractical and politically unpleasant. The OECD opted to enhance performance budgeting systems towards strengthening performance orientation in resource allocation and management (Shah and Shen, 2007: 139-141). Most of these countries focused their efforts on performance management. Shah and Shen (2007) define performance management as the prerequisite for the success of performance budgeting.

## **2.2 Different Budget Systems**

### **2.2.1 Traditional Budgeting**

A traditional budgeting system is based on expenditure control. It is believed that if all expenditures and revenues are accounted for, the budget process will essentially be effective in achieving its objectives. Traditional budgeting lists all expenditures by line-item. This means that the budget shows exactly how much is spent on each item of expenditure such as salaries and wages, transport and equipment. It does not provide any information on the objectives of a particular government department, or any results which are to be achieved by that department. This format of the traditional budgeting system has become known as line-item budgeting.

Moreover, traditional budgeting systems may include incremental budgeting as well as zero-based budgeting. Incremental budgeting is an annual budgeting system which takes the current year's budgeted allowances as the starting point for preparing next year's budget. It presumes that the current year's budget is the most appropriate basis for estimating the following year's budget. With traditional

budgeting there is also a distinct lack of integration between planning and budgeting.

### **2.2.2 Line-item Budgeting System**

In line with the views of McCaffery, the line item budgeting system emphasizes control over the planning and the management elements of the budget. Fourie and Khalo stipulate that this system of budgeting is control oriented. They further argue that this system of budgeting is characterized as incremental as it is based on information on the last completed fiscal year, the current year and the forthcoming fiscal year. Public participation in this type of budgeting will afford the citizens an opportunity to assess service delivery based on the budgeted items (Fourie & Khalo: 2006: 135).

### **2.2.3 Planning-Programming Budgeting System (PPBS)**

This type of budgeting could be seen as an expensive budgeting system and the only time policy makers and public officials realize this fact is at the end of the projected future, especially if the planned activities do not take place. It is, however, argued that this system is particularly advantageous as it emphasizes planning for outcomes which is essential if government wants to move beyond efficiency and management to decisions based on rational decision making (Fourie & Khalo, 2006: 137). In PPBS there is a recognition that public sector organizations are interdependent. Folscher (2007) argues that PPBS attempts to bring clarity about the goals of government and seeks cost-effectiveness by assessing various courses of action.

Diamond (2003) explains PPBS as follows:

- Identification and examination of goals and objectives in each major area of government activity;
- Analysis of the output of a given programme in terms of objectives;
- The measurement of total programme costs, not just for current year but several years ahead;

- The formulation of multi-year expenditure programme;
- The analysis of alternatives to find the most efficient and effective means of attaining programme objectives

(Diamond, 2003: 5).

Folscher (2007) stipulates that the failure of this budget reform approach was due to the lack of training and shortage of skills of the implementing officials. However, the shortcomings of this system were rectified by implementing the zero-budgeting system. This system emphasized planning in order to succeed, and in prioritization and accountability through control elements and other control related measures and mechanisms, to improve accountability at all government levels.

#### **2.2.4 Target-Based Budgeting System (TBBS)**

The TBBS is particularly suitable for local government. This system identifies overall expenditure for government based on revenue estimates that are available and that there is executive control measures in place. According to Reed (2003), TBBS is easily implementable in municipalities because they have to control spending. However, municipalities are also faced with the challenge of unpredictable demands for services by local citizens.

#### **2.2.5 Zero-Based Budgeting System**

In this type of budgeting system, the budget is defined and reformulated from zero on an annual basis (Khalo & Fourie, 2006: 138). It is said that information that is available from previous budgets is disregarded and only figures that are related to the future are considered. This system calls for new information whenever budgets have to be determined each year, which means that old and redundant activities will be discarded when new ones are started. MacGill argues that the key to zero-based budgeting system is that planning and budgeting are done at the same time. However, he emphasized that the failure of zero-based budgeting is the lack of rigour in quantifying decision-packages (MacGill, 2001: 377).

Folscher (2007) identified the following shortcomings of zero-based budgeting:

- It generates masses of paperwork for which there is neither the time nor the human capacity in budgeting systems;
- It is not necessarily true that lower-priority programs will receive less funding or be discontinued: the approach fails to take into account the realities of institutional and public politics that drive budgets;
- It is not self-evident what is maximized if zero-based budgeting is adopted in its classical form. She argues that in this form it is an inwardly focused process that puts emphasis on the priorities of managers. Insufficient attention is paid to mapping decisions to the preferences and priorities of beneficiaries. Like PPB system, zero-based budgeting was also abandoned as a budgeting technique.

(Folscher, 2007: 123).

### **2.3 Budget Reform Process in Australia**

Australia instituted a MTEF, which focused the budget process on changes in strategic priorities within aggregate fiscal parameters. It introduced measures that grant considerable flexibility to the line agencies and that provide them with incentives to identify savings options themselves. The reforms sought to focus attention on outcomes and introduce some form of accountability, although these are not formalized (Compos and Pradhan, 1997: 437). Budget reforms in Australia consist of several, interrelated elements. A cornerstone of the Australian reforms has been a system of forward estimates, or three-year forecasts of the minimum cost of existing policies and program, which are automatically rolled into budgetary allocations if there is no change in policy. South Africa's budget system is also based on this approach.

According to Schick (2001) Australia led the MTEF movement during the 1980s by expanding its forward estimates into multi-year targets that rapidly gained standing as the basis on which spending departments bid for resources and the annual budget is compiled. In the Australian model, MTEF was not linked into the existing budget process. It became the budget process, that is, the means by which government parcels out money to spending portfolios (Schick, 2001: 5). Most of



the expenditure details compiled in the annual estimates were transferred to departments, thereby freeing up the Cabinet for policy work on the aggregates, allocations to the main budget sectors, and the policy changes.

Schick (2001) argued that without the direct involvement of political leaders, the MTEF would be little more than a technical exercise and more a matter of projections than of policy decisions. The reputed success of Australia's reforms spurred an interest in the MTEF. However, in some countries the MTEF is little more than a multi-year projection. In others, it is a technocratic exercise that does not involve strategic decisions by political leaders (Schick, 2001: 7). In the case of South Africa, political leaders are directly involved in the MTEF budget process. Policy priorities are the guiding factor for the MTEF. Through budget policy statements, political leaders are directly involved in the MTEF.

A change in policy results in change of budget allocation. Ministers now allocate the limited time for budget consideration to policy development rather than zero-basing on entire set of appropriations. Secondly, a mechanism for macroeconomic planning reconciles the forward estimates with the target deficit to identify the scope for new spending and savings (Compos and Pradhan, 1997: 437). Thirdly, a system of portfolio budgeting was introduced in Australia as part of its budget reform process. This devolves priority setting to individual portfolios by encouraging and requiring line agencies to themselves identify savings and spending options within their portfolio to meet their net savings target. Finally, while portfolio budgeting and the running cost system devolved authority to line agencies, program management and budgeting was introduced to focus attention on outcomes instead of inputs. This entailed the clarification of portfolio activities into programs, and the introduction of accountability mechanisms by requiring departments to report on the performance of programs within their portfolios (Comps and Pradhan, 1997: 438).

The most recent Australian budget reform, the Accrual Outputs & Outcomes Framework (1999) emphasizes the need for stronger accountability of agencies to departments as well as an enhanced external accountability. Since the early eighties the Australian Government had developed initiatives to make the budget and

management system more results-oriented. Since the mid-nineties there is an increased attention to an integrated, comprehensive reform strategy (Sterck and Scheers: 2003: 8). In 1996, it was decided that an accrual-based outputs and outcomes budgeting and reporting framework would be introduced in the Australian Public Sector. According to Sterck and Bouckaert (2006) the framework which was implemented for the first time in the budget of 1999-2000, focused on managerial responsiveness on the one hand, combined with an outcome-oriented, long-term budget and planning process on the other hand.

The objectives of the accrual-based, outcomes and outputs framework were:

- To provide a framework for better managing complexity;
- To align departmental outputs more expressly with the outcomes government specifies;
- To improve the quality of decision-making within agencies;
- To enhance the transparency of management decisions and activities; and
- To provide a management and accountability system based on indicators of effectiveness and performance (Sterck and Bouckaert, 2006: 5-6).

## **2.4 Structure of Budget Systems in OECD Countries**

In the OECD countries there are different budgeting systems. The first cluster contains budget systems featured by a top-down macro-budget process but a decentralized micro budget process e.g. New Zealand, UK and Sweden. The second structure consists of budget systems that remain rather centralized and characterized by an influential central actor dominating the overall budget process e.g. Netherlands, the United States of America and Canada (Sterck and Scheers, 2003: 9).

### **New Zealand**

In New Zealand the executive budget process exists of two phases: the strategic phase and the initiative phase. During the strategic phase Ministers decide on the general budgetary policy for the coming three years. This results in the submission

of a Budget Policy Statement in Parliament. During the initiative phase Ministers and chief executives prepare budget baseline submissions or vote budget submissions on the one hand and budget initiative submissions on the other hand. Afterwards the Cabinet collectively reviews and discusses the budget baselines and the budget initiatives and decides whether the submissions fit into the general fiscal strategy. Sterck and Scheers (2003) stipulate that Ministers have the freedom to transfer resources between outputs as long as the budgetary baseline is not exceeded.

When the final budgetary decisions are made by the Cabinet, the budget documents are presented to Parliament and discussed on Budget Day. Afterwards the Finance and Expenditure Committee discusses the Budget estimates and refers them for further examination to the competent committees. These committees report back to the plenary and after the third reading, the Appropriation Bill is approved. Members of Parliament have the right to propose amendments to the Vote Budgets, but the Cabinet has a veto power, that cannot be overruled. The New Zealand budget process is thus characterized by a strong executive dominance and a combination of a top-down budget strategy and bottom-up budget submissions (Sterck & Scheers, 2003: 11).

This is similar to the South African budget process. Like the situation in New Zealand, in South Africa Ministers prepare their MTEF budget submissions. In the submissions Ministers list their departmental priorities and budgets. In New Zealand, when the final budgetary decisions are made by the Cabinet, the budget documents are presented to Parliament. Likewise in South Africa, in that MTBPS are first considered by Cabinet and then tabled in Parliament (National Treasury, 2001).

### **United Kingdom**

The 1998 Comprehensive Spending Review introduced a multiyear and outcome-oriented budget process in the UK. Every two years, the budgetary and policy objectives are evaluated and revised during the Spending Review process. The Treasury sets the level of Total Managed Expenditure for the coming three year

period and derives the Departmental Expenditure Limits and the Annual Managed Expenditure. The departments and HM Treasury negotiate Public Service Agreements that set the aims, objectives and performance targets that government is to achieve. Within the boundaries of this Public Service Agreement the departments have managerial autonomy for resource allocation. Sterck and Scheers (2003) conclude that in the United Kingdom budget system, a top-down macro budgetary process is combined with decentralization of financial management and resource allocation to the departments (Sterck and Scheers, 2003: 11).

## **Sweden**

The Swedish budget process can be split up in two large phases: the top-down decision making on the total level of government expenditures and the limits for the 27 expenditure areas; and the bottom-up decision making on the agencies' appropriations. The budget process starts thus with an update and a review of the three-year budget framework by the Ministry of Finance, for the total framework and by the ministries, for their expenditure areas. Based on the recommendations of the Ministry of Finance, the Cabinet then collectively decides on the total government expenditure limit and on the expenditure level for each of the 27 expenditure areas. The decisions of this Cabinet Budget meeting are then approved by Parliament in the Spring Fiscal Policy Bill. Sterck & Scheers (2003) argue that until the decisions are made by the Cabinet Budget Meeting and are approved by Parliament, the budget process occurs very top-down and are rather input-oriented.

Moreover, after the debate on the limits for each of the 27 expenditure areas by the Finance Committee and the discussions on the appropriations by the Select Committee, the budget is approved in the plenary session. The agencies account to the Cabinet on their results by means of an annual report (Sterck and Scheers, 2003: 10).

## **Canada**

The Canadian budget process is characterized by a strong executive dominance. The executive budget process starts with two cabinet meetings in which the broad

budget themes and the key elements are set. The Minister of Finance advises the Cabinet on fiscal and expenditure targets and the President of the Treasury Board gives an overview of the expenditure reallocation and reduction options. Preceding the parliamentary approval process, Parliament discusses the budget during the pre-budget consultation process. The Standing Committee on Public Finance organizes public hearings on the broad budgetary policy and reports the results to the ‘House of Commons’ for debate.

As part of the executive budget process, every Minister can propose new policy initiatives that are discussed in policy cabinet committees. The Ministers compare the different policy initiatives and decide collectively on the most important priorities. They then advise the Prime Minister and the Minister of Finance on their decisions. The Prime Minister and the Minister of Finance then make the final budgetary decisions and introduce the Budget in Parliament. The President of the Treasury Board submits the Estimates and the Reports on Plans and Priorities for each department and agency. After the examination of the Estimates by the Standing Committees, Parliament approves the Estimates (Sterck and Scheers, 2003: 12). The advantages of this budget process is the enforcement of government policy priorities. Policy priorities are most likely to be budgeted for since the executive has a strong dominance. The disadvantage of this system compared to other decentralized systems is that provinces do not have an input into the budget process. This can negatively affect implementation at provincial and local government level.

### **United States of America**

In the United States of America there is a more even distribution of power between the executive branch and the legislative branch as compared with most OECD-countries in which the executive branch dominates the legislative branch. The Congressional Budget Act of 1974 provides for the legislative and the executive branch to formally have their own budgets and the budget procedures which are intertwined in the annual cycle (Sterck and Scheers, 2003: 13). The budget process in the United States may not address priorities of the poor and the distribution of power between the executive branch and the legislative branch could result in

unfocused policy priorities. Priorities of the poor are likely to be addressed at the executive branch where planning takes place.

## **Netherlands**

The budget process in the Netherlands is essentially top-down. The Minister of Finance develops the scenario for the budget process and the budget instructions and sends them to the departments which can then start with the preparation of the budget. The Minister of Finance then provides the Cabinet with an overview of the budgetary and economic expectations and the scope for policy making, by means of a budget submission.. Sterck and Scheers (2003) stipulate that on the basis of this submission, the Cabinet decides on potential budget cuts, the total amount of expenditure for each department and the budgetary space for new initiatives. After that, each department sends the budget submission to the Minister of Finance and discusses the proposal with the Inspection of Finance. Then the decisions are made on the estimated fiscal revenues based on the latest macro-economic forecasts. The macro-budgetary and financial policy is set out in the so-called Miljoenennota which is submitted to Parliament together with the departmental budgets in September. The Miljoenennota and the Departmental Budgets are then discussed and approved by both houses of Parliament. Only the Lower House has the right to amend the budget (Sterck and Scheers, 2003: 12).

The significance of top-down budget processes is budgeting for policy priorities at national level. Policy priorities are drafted by national government and it makes sense for national government to allocate budget for these priorities. On the other hand a bottom-up approach is important for addressing social inequalities. Allowing provincial and local government to have a say in the budget process creates a conducive environment for social inequalities to be addressed. Both approaches are important in the budget process.

### **2.5 Background on Performance Budgeting Framework (PBF)**

Diamond (2003) argues that although elements of programme budgeting were in evidence in the United States prior to World War II, the term performance

budgeting is more clearly associated with the 1950s reforms in the United States, when the Hoover Commission on the organization of the executive branch of the government in 1949 promoted this approach and encouraged its widespread implementation (Diamond, 2003: 4).

The failure of line item budgeting resulted in the adoption of programme budgeting. Programme budgeting focuses on how much has been spent on each function of government, rather than how much has been spent on each type of input (Abedian and Strachan, 1998: 57). But even within programme budgeting, the various components of costs would still be listed under each programme. It is only after the 1990s that governments realized that there is a need for a more results-orientated approach.

Programme budgeting systems were thus refined to incorporate the notion that financial planning and management must be closely interlinked with broader management practices, such as strategic management, organizational management as well as performance and quality management (Abedian and Strachan, 1998: 58). PBF emphasises the need to connect financial planning and broader management. This was not done in the traditional budgeting frameworks.

Effective budgeting is a powerful management tool; and measuring performance of managers brings change and accelerates delivery within government departments and organizations. PBF provides a planning framework in which the performance measurement aspect of budgeting is well suited to measuring efficiency and effectiveness. Efficiency and effectiveness are crucial concepts in PBF. Well-developed budgets allow for devolved authority and accountability, and enable managers to take responsibility for their own performance (Abedian and Strachan, 1998: 66). PBF is essential for all government departments. PBF is different from line item budgeting in that in PBF requires that certain steps are followed.

These steps are:

- When applying PBF, the starting point is the aims and objectives of the department or organization, with a hierarchy of core and supportive objectives;
- These objectives become the focus of programmes and sub-programmes and are therefore used to develop the programme names and programme structure;
- After designing the programme structure the next step will be to develop activities (actions) that contribute to achieving the objectives;
- Resources/inputs used for these activities are identified and costed;
- Performance measures (outputs) and indicators (outcomes) which result from these activities must be defined and quantified;
- After defining performance measures and indicators cash flow must be projected. Cash flow is the monthly allocation of funds out of the total budget; and
- Future resource requirements must be estimated, so that future costs can be predicted and a multi-year budget and delivery framework developed.

(Abedian and Strachan, 1998: 65-66).

In enforcing performance budgeting in government departments, Diamond (2001) suggests the following steps:

- Keep participants focused on objectives. Publicizing these objectives is one approach of creating incentives and pressurising participants to meet these objectives as well as to enforcing efforts to hold them accountable for achieving these objectives;
- Evaluation of performance as a tool to enforce performance effectiveness in meeting objectives must include a feedback mechanism to continuously improve the means to attain the objectives;
- Rewarding good performance and sanctioning poor performance. Establishing clear performance accountability involves firstly a threshold level of basic financial and personnel management systems to be in place to report on performance; and secondly a performance system orientated to linking rewards to performance;



- Greater application of information technology. Improved classification systems to identify programmes, so that costs can be allocated to individual activities, to be composed with the outputs of these activities;
- Moving performance indicators from quantity to quality. The importance of performance indicators has long been recognized in reforms associated with performance budgeting.

(Diamond, 2001: 18).

The above represents PBF and the processes applied by organizations and government departments that implement PBF. But it is a challenge to implement PBF, especially in developing countries, simply because it is a new concept. Managers in the public sector are not used to being assessed in terms of performance. Another challenge is the lack of political will by governments. Political will is crucial for the success of any policy. Although there are challenges in implementing PBF, it is being used by all government departments. However, the pace of its implementation is very slow and it will take some years before managers in the public sector get used to being assessed against their performance. In South Africa, the MTEF is supported by the Public Finance Management Act (PFMA) of 1999. The MTEF and the PFMA are both the driving forces of PBF in South Africa as they put more emphasis on performance assessment.

The PFMA places emphasis on effective and efficient government expenditure, as well as on accountability and transparency (IDASA, 2004). PFMA has stringent financial reporting and information requirements, thereby obligating government to produce the information needed to track and monitor public resources because it emphasises outputs and outcomes. Mr Trevor Manuel, the National Minister of Finance, stipulated in 1998, that the MTEF is one of three broad reforms to the budget process in South Africa. The key features of the MTEF are:

- The publication of three year forward estimates when the Budget is tabled in Parliament;
- A focus on outputs and outcomes of government spending programmes as part of the budget review process;

- A cooperative approach to the expenditure analysis and planning, involving national and provincial treasuries and spending departments;
- More detailed budget information to promote understanding and debate in Parliament and civil society; and
- A budget process aimed at informed political responsibility for budget priorities and spending plans (Manuel, 1998).

A government's budget performance is reflected in its inputs, outputs and outcomes. In order for the performance budgeting framework to be useful it must have the following three E's: economy, efficiency and effectiveness.

Economy refers to government's management of inputs in relation to costs. A budget is economical when the best possible inputs are being secured with the funds available. This means that the cost of inputs must not exceed the budgeted amount. Efficiency refers to how government works with inputs in relation to outputs. A budget is managed efficiently when inputs are used in such a way as to produce the most possible outputs. Effectiveness refers to how government manages outputs in relation to outcomes. A budget is managed effectively when spending brings about the outcomes it set out to achieve (IDASA, 2004). If government's budget performance fulfills all the above it will be called effective budgeting performance.

It is these characteristics of PBF that make it a useful tool for government departments to ensure service delivery. PBF is being implemented in SA. To illustrate its successes and failures, this thesis assesses the implementation of PBS (PBF) and the lessons learnt in the process, by the Mpumalanga Department of Health and Social Services. The purpose of performance budgeting is to relate resources to results and inputs to outputs and outcomes in a complex organisational context. Such a system requires devolved authority, financial responsibility and accountability, and enables managers to take responsibility for their own performance.

PBS / PBF allows for devolution of powers to the lowest levels, from programme manager to the lower level of activity manager. The PFMA stipulates that line managers, as well as financial managers, are responsible for the effective and efficient use of government resources within their areas of responsibility. Performance budgeting ensures that this takes place.

### **2.5.1 Benefits of Performance Budgeting**

Roberts (2003) listed the following as the benefits of performance budgeting:

- Greater policy focus and prioritization in resource allocation, programme planning and management, because bids for resources and their allocations have to be justified in terms of national and sectoral strategies;
- Better coherence between achievement aspirations and resources available, and greater realism in target setting, achieved overtime, through experience of difficulties and the obligation to render account of performance;
- Stronger motivation on the part of line managers and service providers;
- More effective diagnosis treatment of cases of underperformance due to more systematic monitoring and evaluation of results

(Roberts, 2003: XI).

In explaining performance budgeting further, Diamond (2003) argues that there has been a shift of focus in performance budgeting of 1950s and the performance budgeting of the 1990s. The early versions of performance based budgeting focused on organizational components including mission statements, policy goals/objectives, core/sub-services, and activities. In the 1990s, the focus of performance based budgeting shifted to outcomes, service quality, and customer/citizen satisfaction (Diamond, 2003: 11). Performance budgeting of the 1990s is based on strategic planning, financial planning and programmes.

### **2.5.2 Strategic Planning**

Budgeting is essentially a political process, and the strategic planning component constitutes the political decision-making process; which informs the budgeting

process; which in turn informs the budgeting system of policy objectives. Strategic Planning provides policy directions to the formulation of the budget by defining long-term objectives of the organization. These objectives form an agreed set of priorities in the form of policy goals or outcomes which guide the process of resource allocation. In South Africa, strategic planning takes place at all spheres of government, i.e. national, provincial and local. At each sphere, government is responsible for defining a set of strategic goals and objectives in order to achieve certain policy decisions (Shall, 2005: 18).

At the national level, planning is the responsibility of Cabinet. Their main functions are the coordination of objectives, outputs and outcomes. Strategic planning is an important prerequisite to the budgeting system, and represents the first stage of the entire budgeting process. It is also the stage where, given budget constraints, service delivery needs are prioritised. Without this key component, the budget would be reduced to a financial numbers game, largely unrelated to service delivery. This was the case with the previous traditional budgeting process, where there was little or no coordination between strategic planning and the budgeting process (Shall, 2005: 19).

### **2.5.3 Financial Planning**

On completion of the strategic planning process, the financial planning component is implemented, during which detailed allocation of resources required to achieve the objectives, are determined. During this stage attempts are made to link resources with results in accordance with programme goals and objectives. Shall (2005) stipulates that it is the responsibility of the Head of the Department concerned to ensure that outputs are delivered efficiently within the allocated budget. This stage includes defining a detailed programme structure including programmes, sub-programmes, activities and outputs.

### **2.5.4 Programmes and sub-programmes**

Shall (2005) argues that the process of financial planning begins by establishing a programme structure. The framework for the programme structure is defined by the

core and supportive objectives identified in the strategic planning stage. Shall (2005) stipulates that each programme that is identified should be aimed at a specific goal that reflects the mission of the organization, and should take into account all the activities required to reach this goal. The optimal number of programmes needs to be developed, taking into account what is useful for strategic analysis and budgeting. Each sub-programme is made up of activities that contribute to the achievement of each goals (Shall, 2005: 19).

### 2.5.5 Activities, outputs and outcomes

Activities deal with the actual provision of goods and services. Examples of activities for the sub-programme Emergency Medical Services may include an activity of “increasing the number of emergency vehicles”. Shall (2005) stipulates that a number of activities are likely to contribute to the objectives of a number of sub-programmes. Activities take inputs and translate them through action into outputs, which in turn contributes towards achieving outcomes, which are the defined goals of the sub-programmes identified in the strategic planning phase. In short, outputs are the goods and services produced by activities, while outcomes are the effects of those outputs on the community. Table 3.1 illustrates the relationship between activities, outputs and outcomes.

<b>Table 2.1 Relationship between activities, outputs and outcomes</b>		
Activity	Output	Outcomes
1. Distribution of grants	Grants distributed	Reduced mortality rate

Outputs are measurable and there is a relationship between inputs and outputs. Services cannot be delivered without going through this relationship. This is one

way of improving service delivery within governments departments (Shall, 2005: 20 – 21).

### **2.5.6 Costing**

Costing the inputs needed for certain activities is an important part of financial management. Shall (2005) argues that costing is important because if getting value for money is a priority of the budgeting process, then one must know what the cost of service delivery is. Costs are usually divided into operating costs (ongoing costs of delivering a service) and capital costs (the acquisition of a durable asset). Shall (2005) mentions that there are a number of basic methods of costing, examples being resource-based costing, activity-based costing and target-based costing. Performance budgeting critics like Shall (2005) argue that activity- based costing is the most appropriate form of costing for performance budgeting, because it is better able to determine the exact cost of service delivery by linking input costs to activities (Shall, 2005: 21).

### **2.5.7 Medium-Term Expenditure and Delivery Framework (MTEDF)**

Since the performance budgeting system links budgeting to service delivery, it is also important that service delivery plans are included in the medium-term framework. Service delivery plans should reflect policy priorities and allocate finances accordingly. The expanded framework, which includes service delivery plans, is known as a medium-term expenditure and delivery framework. The MTEDF allows planning and implementation to be linked in a dynamic way, while ensuring accountability for delivery over a number of years. Because of the multi-year nature of the MTEDF it is possible to define a delivery timetable, identify the beneficiaries of delivery and monitor delivery performance (Shall, 2005: 23).

## **2.6 Performance Measures and Alignment**

Performance measures are used when trying to measure the productivity of resource use, which can be clearly quantified. Performance measures gauge the

efficiency of translating inputs to outputs. On the other hand, performance indicators are used when trying to measure how effectively outputs are translated into outcomes. Below is the list of measures used during the budgeting process:

- Input Measures – addresses the question of the amount of resources needed to provide a particular product or service. Input measures have been the major focus of traditional budgeting. However, those measures are useful in showing the total cost of providing a service as well as the mix of resources used to provide the service.
- Output Measures – focus on the organizational activities in providing a particular product or service
- Outcomes Measures – address the question of whether or not the service/program is meeting its proposed goals. They are used to evaluate the quality of effectiveness of programs.

Diamond (2003) argues that the above measures have a significant impact on budget allocation and that without these measures budget allocation would be ineffective. On the other hand, Shah and Shen (2007) argue that an effective performance budgeting system depends on reliable performance measurement and reporting. They argue that the construction of a performance measurement and reporting system provides a channel for public officials to reach agreement on program goals and objectives, to discuss and compromise on the selection of performance measures, to address their questions and concerns, and to overcome misgivings about performance budgeting (Shah and Shen, 2007: 147). In line with performance measurements, OECD countries have focused on performance management as a way of implementing performance budgeting.

## **2.7 Performance Management Models in OECD Countries**

Curristine (2005) defines performance management as a management cycle in which programme performance objectives and targets are determined, managers have flexibility to achieve them, actual performance is measured and

reported, and this information feeds into decisions about programme funding, design, operations and rewards or penalties (Curristine, 2005: 131). Performance budgeting scholars like Shah and Shen (2007) describe performance management as the pre-requisite for the success of performance budgeting. They argue that governments that do not manage for results do not budget for results. OECD countries have used performance contracting as a management instrument and a performance approach to budgeting.

Lidbury (1999) defines performance contracting as a range of management instruments used to define responsibilities and expectations between parties to achieve mutually agreed results. He argues that performance contracting is one element of broader public sector reform aimed at improving efficiency and effectiveness, while reducing total costs. OECD countries viewed performance contracting as a useful tool for articulating clearer definitions of objectives and supporting new management monitoring and control methods, while at the same time leaving day-to-day management to the managers themselves (Lidbury, 1999: 7). Below are some of examples of OECD countries that have adopted performance management practices. These countries include Denmark, New Zealand and Sweden.

### **2.7.1 Denmark: Performance Management Model**

Performance management arrangements are in place in all ministries and agencies in Denmark. Performance contracts were introduced in the late 1980s on a pilot basis, but they have now become an established feature of the management of the Danish public sector (Shah and Shen, 2007: 148). It is said that the overall quality of the performance contracts has improved over time, but the quality of the outcome and output descriptions still leaves room for improvement. Agencies annual reports show results achieved relative to targets for all specified outcomes and outputs. It is published three months following the end of each fiscal year.

Moreover, the performance pay system for directors general was introduced in the mid-1990s. The criteria for performance pay is based on achieving the



targets specified in the agencies' performance contracts. Shah and Shen (2007) argue that the Danish performance management system, rather than being regarded as a contractual arrangement, serves more as a formal structure under which ministries and agencies discuss the results to be achieved and the ministries highlight areas they view as especially important and urgent.

### **2.7.2 New Zealand: Performance Management Model**

New Zealand revamped its tenured civil service and made all public positions contractual, on the basis of an agreed set of results. Agency heads are required to negotiate purchase agreements with their ministers and are held responsible for the delivery and reporting of expected outputs relative to targets and budget. Shah and Shen (2007) argue that statements of intent commit ministers to achieving progress towards outcomes. Program management was decentralized at delivery points, and managers were given flexibility and autonomy in budgetary allocations and program implementation within the policy framework and the defined budget. The contractualism version of outputs accountability in the public sector introduced by New Zealand led to significant improvement in the machinery of government and in the fiscal performance of the state sector. Departments have a clearer idea than they used to of what is expected of them, their output is specified and fully costed, chief executives have broad discretion to manage resources and operations, ministers have choice in obtaining outputs, and overall public sector is leaner and more efficient (Shah and Shen, 2007: 149).

### **2.7.3 Sweden: Deregulated Human Resource Management**

In Sweden, directors general of agencies are responsible for recruiting, grading, and dismissing their staff members. There is no civil service in the government as a whole. There is no difference between the labor legislation governing the public sector and that governing the private sector. The Ministry of Finance and Parliament do not have a direct say in pay arrangements and

other conditions of employment for government employees (Shah and Shen, 2007: 149).

#### **2.7.4 Canada: Performance Management Model**

Lidbury (1999) stipulated that a performance contract provides clarity, transparency and specificity in the roles and responsibilities of parties for carrying out the partnership agreement. The performance contract in Canada identifies inputs, outputs and expected outcomes as well as establishes mechanisms for measuring results. Performance contracting is designed to give structure to the demands and expectations of both parties, and the public, for efficient and effective management, value for money, accountability, and mutual agreement on governance arrangements, results and assessment (Lidbury, 1999: 13). Based on literature review on performance budgeting, there is a need for transparency in the budget process.

#### **2.8 Transparency in the Budget Process**

A movement towards greater transparency in the budget process is practiced all over the world (Folscher, Krafchik and Shapiro, 2000: 3). Folscher (2000) argues that the trend is apparent in developed countries, where broad budget reforms adopted in recent years placed great emphasis on transparency. They argue that good governance dictates that the government operations and decisions should be made openly and with the active participation of the people influenced by them. They further argue that the budget is the economic policy document of the government and that for this reason transparency in the budget is important. Below are some of the identified benefits of transparency:

- Early identification of the weaknesses and strengths of policies, thereby promoting necessary reforms. Scholars like Folscher and Shapiro (2000) argue that transparency can contribute to macroeconomic and fiscal stability as it prevents the build-up of a crisis in secret, bringing about smaller adjustments sooner.

- Improved accountability of government. Legislatures, the media, civil society and the public will be able to hold the executive to account if they have information on its policies, practices and expenditures. Elected office holders and public servants may be more likely to act in a responsible manner if their decisions are open to public scrutiny. Holding governments accountable can provide a check on corruption.
- Increased transparency may increase faith in governments and commitment to policy trade-offs. Transparency can thus build social cohesion in the sense that if the public can better understand what their government is doing and why they are doing it, they may have more confidence in that government.
- Improved investment climate. With a clear understanding of government's policies and actions, international and local investors may be willing to invest more resources in a country.

(Folscher, Krafchik and Shapiro, 2000: 5).

The above three scholars argue that there is a need to make connections between transparency and public participation. Transparency and participation are mutually reinforcing and jointly required for better budgetary outcomes. Transparency is a requirement for public debate and participation which, in turn, can lead to more requests for information:

- Involvement of actors outside the executive branch can improve policy and allocation decisions by bringing different perspectives and creativity to budget debates. The need for such participation is strengthened by the legislatures' and civil society's closer contact with communities and interest groups.
- Information may allow legislatures to monitor executive decisions and performance, but if they do not have sufficient opportunity to act on the information they receive, their oversight may be less effective.
- While transparency can stimulate consensus on policy and allocation decisions, this consensus may be prevented or weakened if stakeholders are not able to participate in a debate.

(Folscher, Krafchik and Shapiro, 2000: 5-6).

Given the current trends of corruption in the public sector, transparency in the budget is crucial. One can say transparency is the pre-requisite for performance budgeting. However, transparency in the budget process requires a good legal framework that will ensure compliance and enforcement.

## **2.9 Chapter Summary**

Budget reform is not a new concept; it can be traced back to early 1900 when budgeting was introduced by various governments. In traditional budgets, all expenditure was listed by line-item, which means that budgets showed exactly how much had been spent on each type of expenditure. The aim of the traditional budget process was simply to keep control over all money spent by government (Abedian and Strachan, 1998: 54). Reasons that led to budget reform is increase in oil shocks, low growth and inflation, rising unemployment and escalating fiscal deficit. The lack of data on the costs of particular services made it difficult for countries to link resources and results.

Diamond (2001) argues that these are some of the factors that prompted the restructuring of the budget management systems in OECD countries. This has led to a change in budget focus towards results-oriented or performance based budgeting in OECD countries.

According to an OECD Policy Brief (2004), governments have introduced performance based budgeting for the following four main reasons:

- To improve efficiency;
- Decision-making in budget process;
- Transparency and accountability; and
- To achieve savings.

This Chapter also discussed the need for performance management in the budget process. The link was made between performance management, performance measures and performance budgeting. Curristine (2005) stipulated that the desire to improve government performance has been inspired by increasing spending

constraints within governments. Attention now is no longer on line-item spending but on achieving better results from existing funds. The focus on performance prompted the shift towards performance budgeting. Performance measures gauge the efficiency of translating inputs to outputs. Diamond (2003) argues that these measures have a significant impact on budget allocation and that without these measures budget allocation would be ineffective.

On the other hand, Shah and Shen (2007) describe performance management as the pre-requisite for the success of performance budgeting. He argues that governments that do not manage for results do not budget for results. All these budget reform initiatives have to be based on a solid legal framework for enforcement purposes. It is stipulated that an appropriate legal framework helps to ensure that adequate checks and balances have been established for the budget systems.

## **CHAPTER 3**

### **3. Towards Performance Budgeting in South Africa**

#### **Introduction**

Apartheid left South Africa with high levels of inequality in wealth, income and in access to public services. Although the previous dispensation developed a pool of expertise and structures for financial planning and management, these were concentrated in the Pretoria bureaucracy, leaving corrupt and bloated bureaucracies within local authorities and in apartheid's system of 'independent homeland's - many of which failed to maintain any systems of accounts at all. In South Africa, government budgeting has historically been performed applying the traditional line-item budgeting system. Historically, the budget was designed to address the needs of the minority and created huge inequalities that the current democratic government has to address.

Against this background, National Treasury embarked on an ambitious programme of budget reform. The most compelling reasons for the programme were problems inherent in the budget; namely a rising deficit, poor delivery of services and lack of transparency and accountability. The historical budget system in South Africa contained several weaknesses. Firstly, the previous budget process did not link planning and budgeting; with directorates for each of these functions usually kept separate within the same departments. Planning was seen as a political process and budgeting as a technical exercise. Policies were not required to be costed and in most cases the data and methodology for doing so accurately did not exist (Van Zyl, 2003: 4).

Secondly, budgeting was incremental with small adjustments being made to allocations and with little thought given to the activities being funded or to the long term goals of the relevant department. The focus of attention was on securing more money, not on delivery. Thirdly, prior to the elections in 1994, Parliament had an even smaller role in the budget than it does now. The ability and opportunity for

the public or organized civil society to interact with the budget process was non-existent. Budget priorities were linked to the apartheid plan (Van Zyl, 2003: 4).

Fourthly, the budget reporting format of the previous system focused only on inputs to departments, but did not describe what that money would purchase (outputs) or how such expenditure would contribute to departmental aims (outcomes) (Van Zyl, 2003: 5). Types of expenditure were listed without providing information on the purpose of that expenditure.

Performance based budgeting has improved accountability at all levels of government. This system of budgeting promotes not only communication with citizens but also amongst government institutions; and they are also able to evaluate one another's performance of government machinery. A performance-based budgeting system is characterized by its long-term perspective which emphasizes what will be achieved in the future. Performance indicators with appropriate measurements are set in departmental strategic plans, with financial resources allocated to ensure that they are achieved. In government, members of Senior Management System (SMS) are also required, in terms of the new role of government, to sign performance contracts against which they are held accountable for the performance of their departments in their endeavor to render services to the citizens (Khalo & Fourie, 2006: 132). Like the situation in OECD countries, South Africa introduced the new form of budgeting called MTEF. The introduction of MTEF was aimed at improving the budgetary process to:

- Restructure expenditure with clearly established priorities;
- Identify the actual cost of particular services so that government could move away from the approach of incremental budgeting ;
- Plan for restructuring of expenditure, as shifts in expenditure cannot be replicated from one year to the next; and
- Introduce a more rational approach to resource allocation, by identifying a few priority activities, which would receive adequate value for money.

(Khalo & Fourie, 2006: 133).

### **3.1 Key Decision-Making Legislation, Processes and Institutions that inform the Budget Process in South Africa**

The following are the key decision making legislation, processes and institutions that inform the budget process in South Africa:

- The Intergovernmental Fiscal Relations Act (IGFRA) of 1997 empowered three intergovernmental bodies to strengthen cooperation on budgeting between all spheres of government. The Act clarified the roles of the Financial Fiscal Commission (FFC), the Budget Council, and the Budget Forum in the budget cycle;
- The FFC is an independent body constitutionally established in 1994. It was intended as an expert, advisory body which could serve as a resource for constructing the budget. Its stated purpose is to make recommendations on the budget and intergovernmental financial issues to Parliament, the provincial legislatures, and the Budget Council;
- The Budget Council is a consultative body comprising of political office-bearers from the national and provincial spheres of government. The Council makes recommendations in respect of the Budget to the Cabinet. The core members of the Budget Council are the Finance MinMEC (the Minister and Deputy Minister of Finance and the nine provincial MEC's for Finance). The Council is consulted on fiscal and financial matters affecting provincial government (National Treasury, 2002).
- The Budget Forum is a consultative forum pertaining to local government. In addition to members of the Budget Council, it includes five members of South African Local Government Association (SALGA) and one representative from each of the provincial associations. This forum looks at fiscal and financial matters in respect of local government;
- The Minister's Committee on the Budget (Min Com Bud) is a prominent actor in the drafting of the budget. This is a subcommittee of Cabinet specifically tasked with budget matters;
- Joint MinMecs which are committees comprising of National Ministers and Porvincial MEC's for sectors which deliver on concurrent functions of



national and provincial government. They meet several times every year to identify trends in the sector, set priorities, and discuss budgetary implications of national policies for provincial service delivery;

- The Treasury Committee is the body which evaluates requests from provinces and national departments for additional funds to address unforeseen or unavoidable needs
- The Parliamentary Budget Committee was formed in 2001. The committee was established as an ad hoc committee, with the immediate task of holding hearings on the MTBPS released in November and tabling a report in Parliament

(National Treasury, 2001).

The above plays a crucial role in transforming the budget process through their emphasis on transparency and accountability. All three spheres of government in South Africa are obliged to comply with the rules of these bodies. Failure to do so results in penalties. The very existence of these bodies contributes to improvements in service delivery. Bodies such as SALGA; and legislation such as the Intergovernmental Fiscal Relations Act encourage good governance which in turn contributes to improvements in service delivery. Good governance refers to a situation whereby all three spheres of government work towards a common goal of reducing social inequalities.

### **3.2 Different Stages of the Budget Process in South Africa**

Treasury Guidelines (2001) stipulates that the budget is developed in stages as detailed below:

- The executive identifies medium-term spending priorities;
- National and Provincial Departments prepare their MTEF budget submissions;
- The Macroeconomic and fiscal framework and Division of Revenue is debated between the three spheres of government between July and August of each year, and is reviewed by an extended Cabinet meeting in September of the same year;

- In September and October, MTEC hearings are held where National Treasury meets with the separate departments. MTEC are technical committees responsible for evaluating the MTEF budget submissions of the national departments;
- The MTBPS is published in October every year. It is first considered by Cabinet and then tabled in Parliament;
- The decision stage in November of each year determines medium-term allocations to national votes and to provincial and local government (National Treasury, 2001).

### **3.3 The Link between the MTEF and Budget Preparation in South Africa**

Folscher and Cole (2004) assess the link between the MTEF and Budget Preparations in South Africa. They argue that the initial experience of implementing a medium-term expenditure framework in South Africa, lacked political involvement, and had no clear link with the budget preparation process. In 1997, the government took these shortcomings into account and merged the MTEF and budget processes. These now include the following coordinated activities:

- Initial Policy Review. The review takes place from May to September and includes the following critical steps:
  - May: The Cabinet considers spending priorities.
  - June-July: Technical committees of national, provincial and local governments meet.
  - July-September: The macroeconomic and fiscal frameworks are revised.
  - September: A Cabinet meeting considers and approves the macroeconomic and fiscal frameworks.
- Preparation of the MTEF/budget proposals. Line ministries' proposals must be submitted to the Ministry of Finance by August 2, structured to clearly identify the proposed policy changes and to include the following items:

- A baseline medium-term allocation. The resource envelope used to determine this baseline consists of the two MTEF forecast years prepared the previous year.
  - Identified savings and reprioritization, within the baseline allocation.
  - Program option that propose changes to the medium-term baseline allocation (for example new programs, change in the level of output, change in implementation schedule of a program). These options should be related to the strategic priorities of the line ministry. For non-recurrent expenditures, estimates should cover five years (two years beyond the MTEF period).
  - Various relevant documents (for example, personnel, analysis of risks and contingent liabilities).
- Review of proposals. During August and September, the provincial and national Medium Term Expenditure Committee, composed of senior officials from the Ministry of Finance and other ministries, evaluates the MTEF-budget submissions of line ministries and makes recommendations to the Ministry of Finance.
  - Submission to Cabinet. The Ministry of Finance submits to Cabinet the draft Medium Term Budget Policy Statement and adjustment estimates. After Cabinet approval, these are tabled in the Parliament of South Africa at end of October, to inform the policy debate but not as a binding document. The draft includes chapters on growth; economic policy and outlook; fiscal policy and budget framework, including a medium-term fiscal framework; taxation; sectoral priorities for the medium-term; and provincial and local government finance.
  - Finalization. In early November, after Cabinet approval, the MTEF allocations to ministries and for conditional grants to national government are communicated through allocation letters by the Ministry of Finance. On that basis, line ministries prepare their draft MTEF-budget during November and December, which includes, under the same format, the estimates for the coming budget year and indicative projections for years

two and three of the MTEF. The complete MTEF-budget is tabled in Parliament in February.  
(Folscher and Cole, 2004).

The above steps are very important because policy priorities are linked to the budget process. This is different from the pre-1994 budget process. Pre-1994 the budget process was focused only on minority priorities and now the budget process focuses on priorities of the majority of people. This will improve service delivery because government's focus is on fulfilling the needs of the poor.

### **3.4 MTEF as a Budget Reform Initiative in South Africa**

The MTEF consists of a top-down estimate of aggregate resources available for public expenditure. MTEF is a rolling process repeated every year and aims at reducing the imbalance between what is affordable and what is demanded by line ministries. The MTEF does this by bringing together policy-making, planning, and budgeting early in the budgeting cycle, with adjustments taking place through policy changes. The key to MTEF is that it links budgets with the policy choices made and improves accountability, and the predictability of funding (MTBF, 1998). Therefore, this study assesses the changes that budget reform brought to the South Africa public. The legal framework in South Africa played a crucial role in terms of changing the budget system in South Africa.

An appropriate legal framework helps to ensure that adequate checks and balances have been established for the budget system. In South Africa, the Constitutional Court and independent bodies such as the Human Rights Commission, are also given, by law, a role in overseeing government's budgeting. A legal framework that clarifies the roles and responsibilities of the executive and legislative branches in the budget system, and that of independent institutions, is essential to establishing accountability. Furthermore, a legal framework should also establish the rules and regulations that guide the budget decision-making process and the management of government revenue and public expenditure. A country without a legal framework within which it budgets can lead to a lack of service delivery. A

legal framework creates a platform for departments to comply with the laws. Compliance with the mandate of government leads to attainment of policy priorities.

### **3.5 Legal Framework for Budget Transparency in South Africa**

The South African legal framework can be described as sound and very enabling with regard to transparency and participation. Important are:

- Constitutional requirements governing revenue funds, the division of revenue, budgets, treasury control, procurement, government guarantees, provincial and municipal taxing and borrowing. The South African Constitution entrenches, in principle, a degree of transparency in budgeting and financial management. Further national framework legislation has been introduced to translate this principle into budget practice;
- The requirements of the PFMA and the Treasury Regulations published in terms of the Act. As an important legislative cornerstone, the PFMA of 1999 sets stringent transparency requirements, including regular reporting and the assignment of accountability. Subsequent legislation has extended the requirements of the PFMA to the provincial sphere of government;
- In spite of significant progress, there continues to be a lack of clarity around the budget amendment powers of the legislature. The legal basis of transparency requirements for the executive is also not comprehensive enough.

(Idasa, 2000).

Furthermore, the Constitution guarantees the independence of the Auditor General. The PFMA extends this mandate to include reports to not only account for funds used, but also to report on the efficiency and effectiveness of spending. Other important developments in the legal framework include the introduction of the MTEF in 1998, the Medium Term Budget Policy Statement (MTBPS) in 1997, negotiation structures and legislation such as the Intergovernmental Fiscal Relations Act, the Financial Fiscal Commission (FFC) and its enabling Act and an annual Division of Revenue Act. Institutional arrangements, like the Budget

Council, the MTEF budget process and the strict assignment of accountability under the PFMA, represent improvements in practice to enforce constitutional roles and responsibilities.

### **3.6 Linking Policy to Budgetary Allocation**

One of the most difficult tasks in budgetary management is to ensure that the budget adequately reflects government policies and priorities especially when it comes to social delivery. Traditional budgeting processes which focus on incremental inputs results in resource inputs being disconnected from the delivery of services. That is a contributory factor to the service delivery crises experienced in Africa. Recent efforts in Africa have focused primarily on the development of MTEF as a tool for resource allocation. However, in practice there continues to be a disconnection between the resulting MTEFs and the adopted budgets.

The MTEF approach is essential to establishing the medium term nature of public spending which is the essential strategic framework of performance budgeting. In a resource restricted environment, which is the case in all less developed countries, it is not possible to implement all policy priorities in any one year. Budgetary management structures focused on outputs must be conceived in a medium term context (McGill, 2001). More recent forms of performance budgeting, which have been developed over the last fifteen years, aim to establish a tightened relationship between funding and performance. The South African government's broad objectives are to grow the economy, advance social development and achieve greater equity in society. The medium-term plans of departments are informed by these broad objectives, with specific output and targets set out in programmes and sub-programmes. The broad objectives of national departments are set out in their strategic plans.

Strategic plans normally cover a period of 3 – 5 years. The revision of strategic plans must be linked to revised priorities and new programme structures. According to Treasury Guidelines (2006), achieving the objectives that are set out in the strategic plan requires solid linkages between planning and budgeting and more rigorous evaluation of budget proposals (Treasury Guidelines, 2006: 4). One

of the main reforms in the 2002 budget process was the integration of strategic plans into the budget process. Van Zyl (2003) argues that the MTEF provides a solid framework for the integration of strategic planning and budgeting. The agreed three-year expenditure envelope and policy priorities create an environment of certainty in which departments can prepare strategic plans and budget (Van Zyl, 2003: 15). Moreover, published strategic plans also increase the transparency and accountability of government departments to Parliament. It enables Parliament to better assess proposed programmes and delivery.

Planning and budgeting must be intertwined in order to achieve set goals and objectives of any government department. A Commonwealth Secretariat report defines planning as the logical organization of activities towards the achievement of national objectives, while budgeting is the financial representation of this plan (Commonwealth Secretariat, 2005). The Secretariat argues that the budget should reflect overall economic policy. The multi-year budget should be based on a medium-to-long term framework. This greatly enhances predictability in departmental allocations and has positive impact on planning and execution within government. This is related to the South African budget system. In South Africa planning and budgeting are intertwined but achieving set goals is still the impediment to solving social inequalities. The reason for this lack of service delivery relates to lack of managerial capacity in most government departments.

Folscher and Cole (2004) also argue that an effective link between policy and budgeting is necessary. Having a budget that is implemented as planned will not result in policy effectiveness if budget plans do not reflect priorities. Folscher and Cole's (2004) research discovered that this budgeting failure occurs when there are weak linkages between budgeting and policy-making, such as when they are conducted in separate institutions, or separate structures in the same institution, or are not linked in time. This is still the scenario of most government departments in South Africa. Departments like Correctional Services, Defence, Home Affairs, Health and Social Development always receive qualified audit reports from the Auditor-General. This might be the result of weak linkages between the policy and budgeting. According to Folscher and Cole (2004), different countries implement

different systems, to ensure tight linkage between policy and budgeting (Folscher and Cole, 2004: xviii).

They further point out that other countries have separate policy framework processes, which are then funded through the MTEF and budget process, and are linked through a range of mechanisms, including budget policy papers, the involvement of sector working groups in the budget process, and public expenditure reviews. It is proven by researchers like Folscher and Cole that an effective link between policy and budgeting improves budget credibility from a governance perspective (Folscher and Cole, 2004: xix). Both these scholars have noted that improved budget planning on its own is not sufficient – it must be accompanied by systems that ensure disciplined use of resources and improved incentives for delivery. This is true, there is a need for a sound managerial capacity in order for planning and budgeting to achieve set goals and objectives.

### **3.7 Multi-Year Budgeting System**

Fourie and Khalo (2006: 139) argue that in the past budgets were prepared on a year-by-year basis whereby short budgets were easy to prepare and manage and are effective for short term planning. With the growth of governments and thus the increase in budgets, a need to plan on a long-term basis arose. In an attempt to address this particular problem, the South African government introduced a multi-year budgeting system. South Africa adopted a rolling budget system in 1998 called the Medium Term Expenditure Framework (MTEF). It allows the government to plan its spending over a three-year horizon in line with its medium-term policy priorities.

The MTEF in South Africa is supported by the Public Finance Management Act (PFMA) of 1999. The South African approach has placed greater emphasis on political involvement throughout the process than is the case in many other countries (Van Zyl, 2003). The MTEF has endeavored to involve politicians in overseeing and managing the entire process, for the first time creating a link between policy planning and budget drafting. In ensuring implementation, the Treasury took the lead in introducing and coordinating the MTEF process. The



MTEF was implemented across all departments as opposed to a focus on getting it right in some sectors (Van Zyl, 2003).

The introduction of the MTEF in South Africa was as a result of a continuous realization of the shortcomings of the short-term budgeting method prior to 1997. The MTEF is also based on the premise that managers will have longer planning periods and as such be able to manage the allocated financial resources more effectively and efficiently (MTEF Handbook, 1997: 5). The budget reform has resulted in greatly improving service delivery in South Africa. Legislators are now able to debate the trends in spending and the direction in policy.

With reference to departments, there is a greater political involvement in making resource allocation decisions based on strategic priorities. Expenditure is linked to delivery and outcomes by ensuring that resources are allocated to what will be delivered and identifying the actual costs of providing services (Walker and Mengistu, 1999: 32). This three-year rolling budget framework means that departments can plan and prioritise with greater certainty about future resource allocations than in the past. With reference to Mpumalanga Department of Health, there is also greater political involvement in making resource allocation decisions. This happens through the provincial budget statement. The three-year rolling budget framework of the department ensures proper planning in terms of resource allocations. It also provides Parliament and civil society with clear signals of government's spending intentions. In the 1998 medium term budget policy statement it is stipulated that the three-year spending projections allow parliament, institutions of civil society and particular interest groups to evaluate Government's reconstruction and development goals and objectives in relation to envisaged spending plans (MTBPS, 1998).

However, there are still disadvantages to this budget reform as it fails to solve problems that have been identified from the previous budgeting system. The budget reform process must deal in practical ways with the challenges of South Africa's fiscal environment:

- A cooperative governance framework in which key policies and their implementation are managed jointly by national and provincial governments;
- The translation of agreed policy goals into delivery of public services;
- The need to make choices so that resources are used to maximize Government's reconstruction and development aims, meet basic needs and ensure distribution;
- The promotion of democratic accountability and greater transparency and understanding of the nation's budget (MTBPS, 1998).

The fact that MTEF allocations are made a number of years in advance can be seen as incremental budgeting. Khalo and Fourie argue that the MTEF budgeting system was supposed to eliminate the issue of rollovers where it would not be necessary for departments to ask for rollovers of unspent funds. Currently in South Africa departments are still required to request for a "carry-over" of unspent funds by way of rollovers into the following financial year. This nullifies the objective of the MTEF process. These challenges underscore the need for a coherent vision of the budget system.

Against this background, the challenge that remains is ensuring that public funds are spent efficiently and that services are delivered. Recent reforms include the tabling of departmental strategic plans to Parliament and the relevant Provincial Legislatures. According to the Intergovernmental Fiscal Review (2003), these plans contain the service delivery objectives and the specific output targets for each programme, alongside the resources that have been appropriated. These reforms aim to improve service delivery and enhance accountability (IFR, 2003: 25). What this means is that, by setting out details on outputs delivered and outcomes accomplished, the annual reports published at the end of each financial year will enable Parliament and Legislatures to better assess whether Government gets value for its expenditure.

According to Chaponda (2004) the MTEF has been widely promoted as a useful tool for making budget decisions within a medium term perspective. The MTEF

links policy, planning and budgeting over a three year period and forces government planners to take a longer term view of their policies as opposed to the previous focus on annual budgets (Chaponda, Cole, Schoch & Gadsden, 2004: 2). The MTEF has become an important feature of budget reform not only in South Africa but in Africa as a whole. The introduction of MTEF in 1997/98 was a central feature of the reform programme but several other steps were important to achieving the fiscal stability currently enjoyed by the country (Chaponda, 2004: 2).

Before budget reform, the South African government was faced with the following challenges: large budget deficit, inflation of about 15% and a social spending programme that largely excluded the majority of South Africans. There was a need for a new budget structure to solve these problems in South Africa. The key highlights of budget reform in South Africa is the roll-out of a new intergovernmental system that requires all three spheres of government to formulate and approve their own budgets, the introduction of three-year rolling spending plans for all national and provincial departments under the MTEF, new formats for budget documentation that include a strong focus on service delivery information, and the enactment of new financial legislation (Chaponda, 2004: 10).

The MTEF was seen as a mechanism for ensuring that spending agencies explicitly consider how to match planned spending with their policy priorities, and for promoting integration of the planning and budgetary processes. McIntyre, Baba & Makan (2000) mentioned the following advantages of budgeting over a long term horizon:

- Permits policy development to be linked with resource over time;
- Creates a predictable medium-term planning environment; and
- Provides a framework for assessing priorities

(McIntyre, Baba & Makan, 2000/01: 7).

### **3.8 Chapter Summary**

The link between policy and budgeting has been highlighted as one of the important factors in budget reform. Folscher and Cole (2004) argue that an

effective link between policy and budgeting is necessary. Having a budget that is implemented as planned will not result in policy effectiveness if budget plans do not reflect priorities. They argue that budget failure occurs when there are weak linkages between budgeting and policy-making. An effective link between budgeting and policy improves budget credibility. The link between budgeting and policy can be done through the MTEF. The MTEF approach was identified as essential to establishing the medium term nature of public spending. The introduction of the strategic framework in budget process is one element of implementing performance budgeting. Van Zyl (2003) argues that the MTEF provides a solid framework for the integration of strategic planning and budgeting. Van Zyl (2003) further argues that planning and budgeting need to be intertwined in order to achieve set goals and objectives of any government department.

This Chapter also discussed the MTEF as one of three broad reforms to the budget process in South Africa. The key features of the MTEF are:

- Publication of three year forward estimates when Budget is tabled in Parliament;
- A focus on outputs and outcomes of government spending programmes as part of the budget review process;
- A cooperative approach to the expenditure analysis and planning, involving national and provincial treasuries and spending departments;
- More detailed budget information to promote understanding and debate in Parliament and civil society; and
- A budget process aimed at informed political responsibility for budget priorities and spending plans (Manuel, 1998).

The budget reform has improved service delivery in South Africa. Legislators are now able to debate the trends in spending and the direction in policy. With reference to departments there is a greater political involvement in making resource allocation decisions based on strategic priorities. Expenditure is linked to delivery and outcomes by ensuring that resources are allocated to what will be delivered and identifying the actual costs of providing services (Walker and Mengistu, 1999: 32).

This three-year rolling budget framework means that departments can plan and prioritise with greater certainty about future resource allocations than in the past.

With reference to Mpumalanga Department of Health, there is also greater political involvement in making resource allocation decisions. This happens through its provincial budget statement. The three-year rolling budget framework in the Department ensures proper planning in terms of resource allocations. It also provides Parliament and civil society with clear signals of government's spending intentions. In the 1998 medium term budget policy statement it is stipulated that the three-year spending projections allow Parliament, institutions of civil society and particular interest groups to evaluate Government's reconstruction and development goals and objectives in relation to envisaged spending plans (MTBPS, 1998).

## **CHAPTER 4**

### **4. Case Study – Performance Budgeting in the Chief Directorate: Health and Social Services of the Province of Mpumalanga**

#### **4.1 Background**

Mpumalanga is the second smallest of the nine provinces of South Africa. According to the Population census 2001 and the South African Health Review 2002, Mpumalanga has a population of 3 122 990. From this total provincial population, an estimated 90% is wholly dependent on government provision of all their health services. Mpumalanga province is ranked the 3<sup>rd</sup> most rural province in the country, with 60.9% of its total population living in rural areas and only 39.9% living in urban areas. It is a new province formed from the splitting-up of the former Transvaal Province during the demarcation of provincial boundaries on the advent of the Interim Constitution of South Africa in 1994.

The Mpumalanga Department of Health and Social Services was previously a division of the Department of Health, Welfare and Gender Affairs. In 1999, the Department was established to focus on health services only. The vision of the Mpumalanga Department of Health is to obtain “the optimal well being of all inhabitants of the province”. (Department of Health, 2000: 3). Its mission is “to ensure the provision and promotion of transparent health services that address the basic needs of inhabitants in Mpumalanga through a decentralized holistic primary health care approach in a caring and gender sensitive manner in order to develop self reliance safe environment”(Department of Health, 2000).

The Mpumalanga Department of Health is a division of South Africa’s national health system. Its policies are therefore shaped and influenced by the National Department of Health. The National Department of Health has, for the past 10 years and in consultation with Provincial Departments of Health, been engaged in the process of developing a National Health Information System for South Africa (Mbananga & Sekokotla, 2002: 6). The aim of the Plan is to develop a system that provides information for health service monitoring, evaluation and planning.

Mpumalanga has established health information systems at both provincial and district level. Mpumalanga Province also shares international borders with two countries vis., Mozambique and Swaziland.

Due to its location, the Province faces an influx of patients from both the neighboring provinces as well as the two neighbouring countries. Mpumalanga consists of three Health Districts, called Ehlazeni, Nkangala and Gert Sibande. Therefore all provincial, regional and district structures in Mpumalanga had to be newly constructed or adapted from those of the former Eastern Transvaal region. The Health portfolio in Mpumalanga is administered by the Chief Directorate: Health which falls under the Department of Health, Welfare and Gender Affairs (DHWGA, 2005).

#### **4.2 Overview of the Department of Health and Social Services**

The Department of Health and Social Services in Mpumalanga inherited a health system which was fragmented, inaccessible to the majority of the citizens of the Province; and was also curative oriented and hospital based (DHWGA, 1997). The hospital based, curative health services consumed the bulk of the health resources of the Province at the expense of preventative and promotive health services. As a result, patients with preventable conditions overloaded the hospital services. The overloading of hospitals by patients with preventable conditions created a vicious cycle which led to a greater demand for more hospitals.

According to DHWGA (2007), health care was available to only a small number of the population, mainly those with the ability to pay and with easy access to hospitals and other facilities which were situated mainly in the cities and urban areas. This unequal distribution of health facilities led to disparities in health care coverage. There was a need for a new health system that would accommodate the majority of the population. As a response to this health inequality, the Department adopted the following goals and objectives as a form of reform.

### **4.3 Goals and Objectives**

The focus of the Chief Directorate: Health and Social Services is to improve the manner in which health services are delivered. In order to achieve this, the broad goals of the Chief Directorate, as noted in DHWGA (1997) are:

- Designing a health service delivery system which can reach the majority of the people;
- Employing measures to prevent and treat preventable diseases and conditions;
- Redirecting the thrust of health in the broader context of development, and
- Providing a caring, compassionate service

In order to achieve these goals and transform the health system into a comprehensive and integrated one, a strategy based on Primary Health Care (PHC) is being implemented. The first step of the strategy has been to restructure the Chief Directorate: Health to decentralize health services to districts. Mpumalanga Province adopted PHC as the main strategy for developing and promoting the health of communities using its district health system as a vehicle for facilitating its implementation.

### **4.4 Structure of the Chief Directorate: Health and Social Services**

Like all Departments operating under a multi-year budgeting system, the Department of Health budgets according to programmes. The budget programmes are as follows:

- Programme 1: Administration

This programme mainly caters for Head Office management support staff.

- Programme 2: District Health Services

This programme caters for district hospitals; community health centres clinics and mobile clinics.



- Programme 3: Emergency Medical Services

This programme provides emergency medical care.

- Programme 4: Provincial Hospital Services

This programme deals with regional hospital services and caters for Ermelo, Themba and Philadelphia hospitals.

- Programme 5: Central Hospitals

This programme provides services of a highly specialized nature. It caters for Rob Ferreira and Witbank hospitals only and is partly funded through a conditional grant.

- Programme 6: Health Sciences and Training

This programme coordinates nursing training, management of bursaries and in-service training of all other categories of staff.

- Programme 7: Health Care Support Services

This programme caters for laundry services at the regional laundries at Bethal and Middelburg Hospitals.

- Programme 8: Health Facilities Management

This programme is responsible for all construction and maintenance work relating to physical facilities of the department.

- Programme 9: Social Assistance

This is now treated as a conditional grant. It provides for the administration and imbursement of social assistance grants and social relief of distress.

- Programme 10: Social Welfare Services

This programme provides and supports the delivery of welfare services by registered implementing agencies.

- Programme 11: Development and Support Services

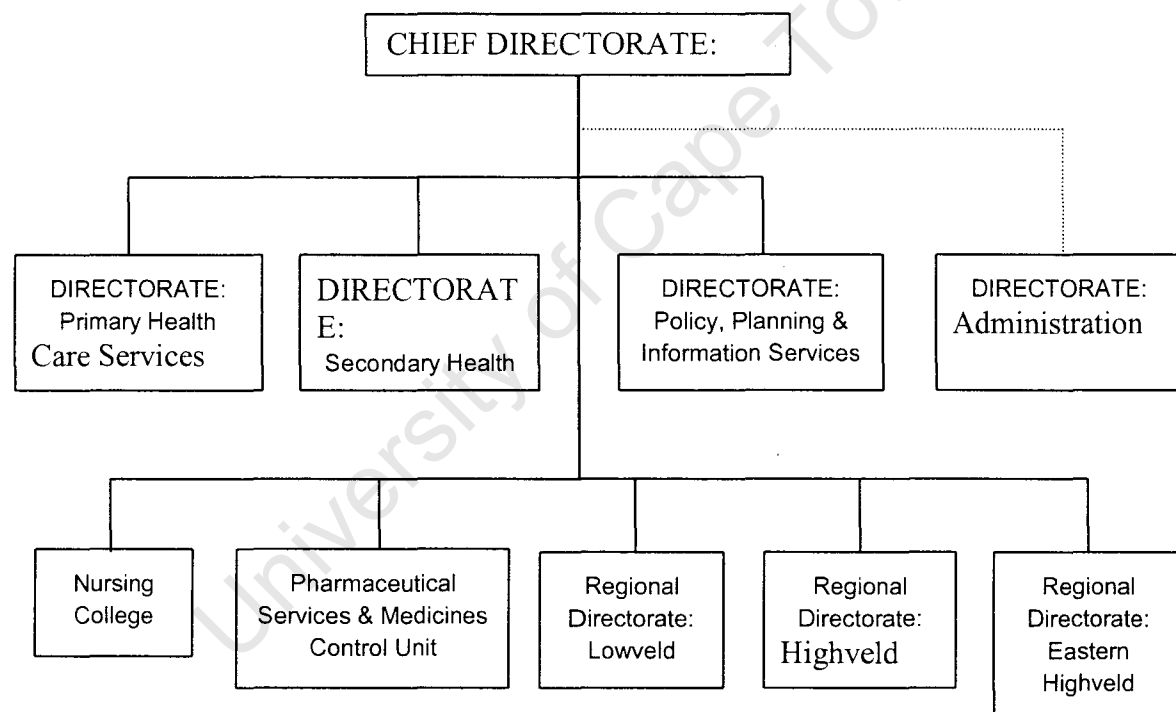
This programme aims to reduce poverty and the impact of HIV and AIDS through sustainable development programmes.

- Programme 12: Population Development Trends

This programme seeks to research, analyse and interpret population and development trends to inform programmes, services and strategies  
(Pasha, 2005/06)

### Department Organogram

**Figure 4.1 The organisational structure of the Chief Directorate: Health**



Source: DHWGA (1997), Primary Health Care in Mpumalanga: guide to district-based action, Durban: Health Systems Trust

The Department of Health in Mpumalanga has two components: a health component and a social component. For the purpose of this research, the focus will be on the health component. The social component consists of the following four programmes:

- Social assistant grant;

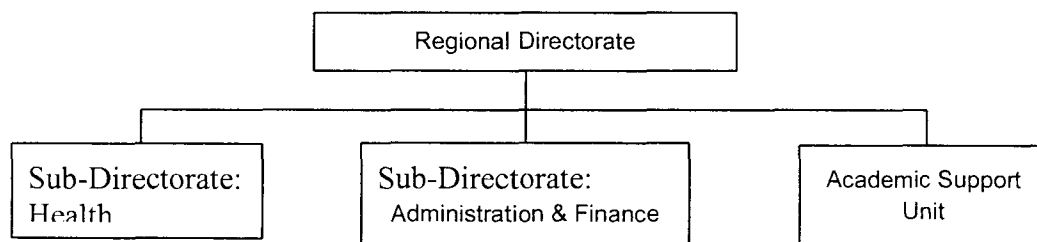
- Social welfare services;
- Development and support services; and
- Demographics

### **Social Services Component**

Demand for social welfare services is increasing and this trend is not consistent with resources available to address the needs of many communities in the Province. As a result the key service delivery components have shown tendencies of over-spending which indicates that there needs to be a radical change in budgetary allocation over the next MTEF period (Strategic Plan, 2005/06: 14). One of the strategic objectives of the National Department of Social Services is “improving service delivery in social security”. This move will provide opportunities for the social welfare programmes in Mpumalanga mentioned above, to get the necessary focus and resources that would result in accelerated service delivery. Although addressing the issues of social security is a priority there are other broad policy priorities within the Department of Health.

In attempting to offer social services to the poor, the Department has set a target of 501 722 beneficiaries of different grant types. By the end of the financial year the Department had exceeded its target in terms of providing grants to the poor. The composition of Mpumalanga’s Regional Health Offices (RHOs) is illustrated in Fig 4.2.

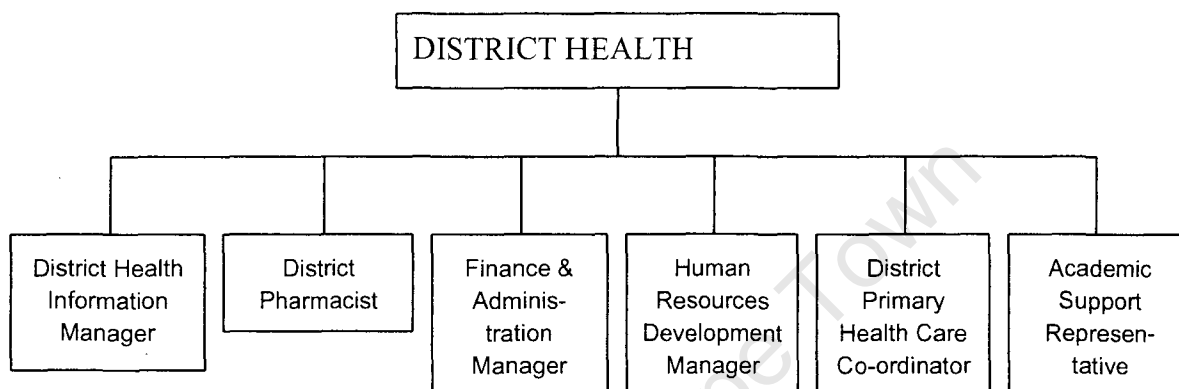
**Figure 4.2 Composition of Regional Health Office**



Source: DHWGA (1997), Primary Health Care in Mpumalanga: guide to district-based action, Durban: Health Systems Trust

Each region is further divided into a number of districts which are managed through the District Health Office by a District Health Management Team (DHMT). The DHMT is responsible for the provision and management of district health services. Its focus is to plan, deliver and manage integrated health care services. Figure 4.3 below shows the structure of the DHMT.

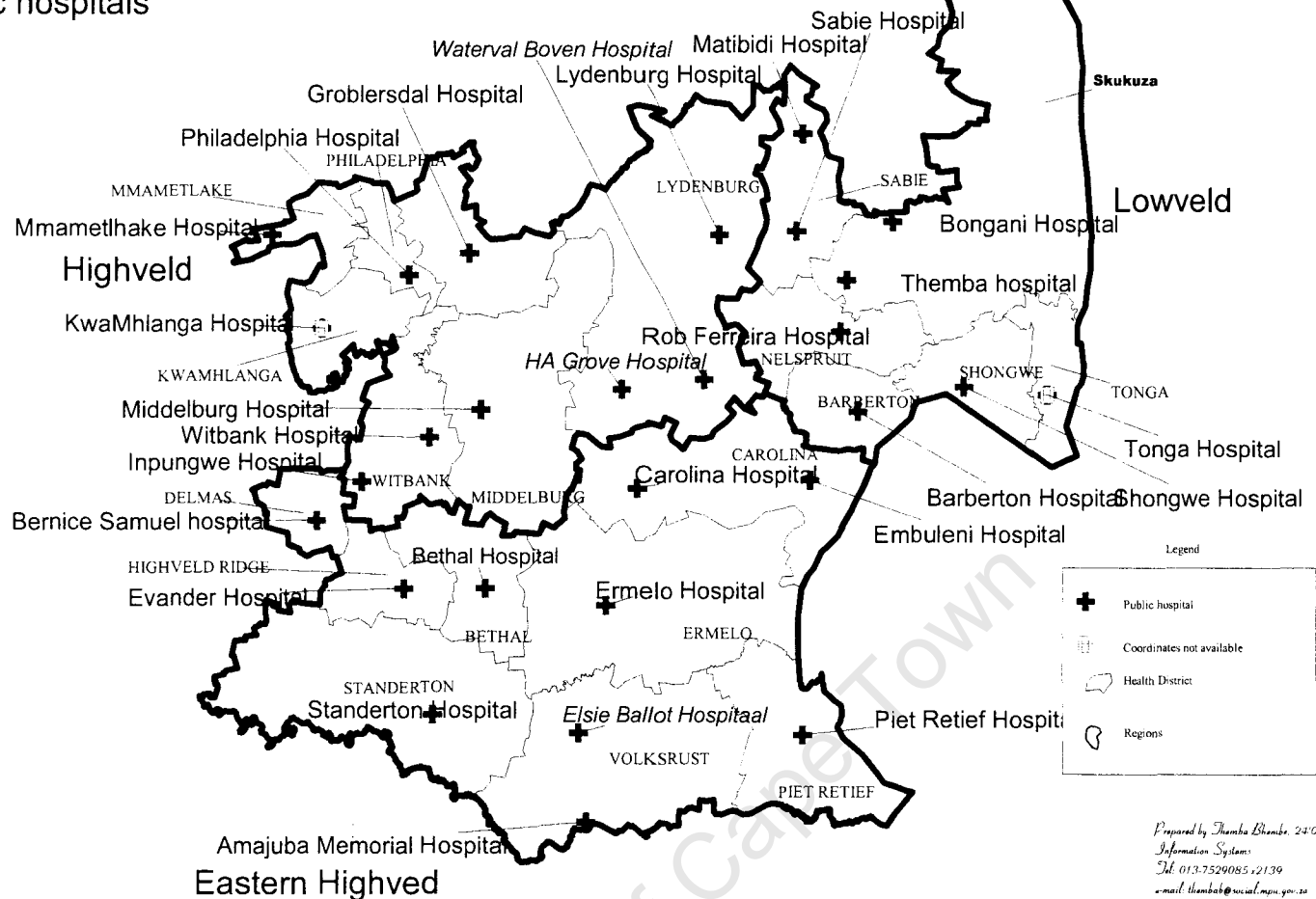
**Figure 4.3      Composition of a District Health Management Team**



Source: DHWGA (1997), Primary Health Care in Mpumalanga: guide to district-based action, Durban: Health Systems Trust

# Mpumalanga Province

## Public hospitals



This map is designed to give the reader an idea of how the 16 Health Districts were structured.

Members of the DHMT are:

- District Health Manager
- District Primary Health Care Co-ordinator
- Administration and Finance Manager
- Health Information Manager
- Human Resource Development Manager
- District Pharmacist
- Academic Support Representative

The District Health Manager is responsible for the development, provision and supervision of health services in the district, including monitoring and evaluation of coverage, efficiency and effectiveness (DHWGA, 1997: 32). The District Health Manager plays a key leadership, managerial and technical role in co-coordinating district health programme planning and implementation. The functions of the

district health office is ensuring health service delivery to the communities; ensuring proper management and utilization of resources; managing and developing personnel; maintaining and managing the district health information systems. The basic aim of restructuring in this directorate was to decentralize decision-making, resource control and service coordination to the district level and thus closer to the community.

#### **4.5 The Research Findings**

The paragraphs below discuss the findings of this research. The findings are based on the comparison of the literature review and the views of the public servants interviewed. The findings are based on the research questions asked during the interview process.

#### **4.6 Health Department Service Delivery Structure after 1994**

To ensure delivery, the Department ensured that activities are in line with strategic goals of the Department. The interviewee from the Department of Health in Mpumalanga mentioned that in terms of the reporting structure, programme managers reported to Premier's Office as they were appointed by the Premier. On the other hand another interviewee stated that goals and objectives were set by the Department but because budgeting was incremental, the status quo tended to dominate.

In an attempt to capacitate the Chief Directorate: Health, the interviewee stipulated that there was training conducted by the Provincial Treasury. The training was based on the implementation of the PFMA. This training was the result of the introduction of the Health Financial Management Grant – a grant specifically allocated for the training of health departments.

In terms of monitoring and evaluation of programmes, one of the interviewees pointed out that there has been monitoring and evaluation in place but not to the extent or quality to which it should be. Managers would report to the Head of Department and explain what they should achieve. However, the quality of reports

and extent of evaluation was not up to standard. The Premier's Office, Provincial Legislature and Provincial Treasury has an oversight role over Departments in Mpumalanga. The interviewee states that Departments were encouraged to improve their Monitoring and Evaluation mechanisms in an attempt to improve the quality of reporting. However, another interviewee pointed out that there was only annual reviewing of expenditure which means that it was difficult to review expenditure during the year.

#### **4.7 How Does Government Define Performance?**

Curristine (2005) argues that performance means the results of activities carried out in relation to the purposes being pursued. The desire to improve government performance has been inspired by increasing spending constraints within governments. More attention now must be given to achieving better results from existing funds (Curristine, 2005: 129). In the traditional public sector bureaucracy, performance was driven by ensuring compliance with set rules and regulations, controlling inputs, and adhering to the public sector culture. There was no focus at all on results.

Curristine (2005) argue that performance information is important for governments in assessing and improving policies:

- In managerial analysis, direction and control of public services;
- In budgetary analysis;
- In parliamentary oversight of the executive, and
- For public accountability-the general duty on governments to disclose and take responsibility for their actions

(Curristine, 2005: 129)

The public servants that were interviewed had an understanding of the importance of performance within government departments. It became clear that almost all Directorates within the Department of Health and Social Services are using performance as a standard for improving service delivery.

#### **4.8 How Performance Budgeting Arose in Mpumalanga Department of Health**

Performance Budgeting arose from the AFReC unit which is a research institution, the Health Systems Thrust (HST) and Kaizer Foundation funding at the University of Cape Town's Business School in conjunction with the Oliver Tambo Fellowship Programme on Health Financing. It was started by Professor Iraj Abedian, with the software development coming from Sebastian van Heerden. It has been "rolled-out" to the Mpumalanga District Health Finance teams. It has taken districts from the position of having their own budgets essentially worked out for them, to a situation where they competently decide their own budget, at detailed item level, per hospital and clinic. District municipalities also cashflow their budgets.

#### **4.9 Budgeting Structure Prior to Performance Budgeting in Mpumalanga**

The Chief Directorate: Health of Mpumalanga had inherited a fragmented health system which was inaccessible to the majority of the population. The budgeting system of the Chief Directorate: Health of Mpumalanga, prior to the introduction of reforms, was based on programme budgeting, whose structure consisted of two programmes presented in line item format. The Mpumalanga Department of Health was no different in its budgeting style from most government departments, in the sense that there was always a large discrepancy between what was said to happen and what actually happened. It is said that in this type of budgeting funds were allocated according to specific programmes in such a way as to realize the aims and objectives of the Chief Directorate: Health (DHWGA, 1997: 35).

The programmes within the prior budgeting system were broad and there were no clearly defined objectives. The following have been described as problems with the old budgeting system in the Chief Directorate: Health in Mpumalanga. The budgets of district municipalities often did not comply with Head Office thinking. Head Office generally did the budgeting for the branches, and there was no ownership of the result. Budgeting in those days worked on broad percentage principles and more often was incremental, with no justification for the increments.



In 1998, with the guidance of AFReC, a Performance Budgeting System management group was set-up to oversee the implementation of a Performance Budgeting System. The starting point was the strategic plan for the department, and the objectives of each Directorate and Sub-Directorate. Members of the management group decided to first concentrate on the District Health Services (DHS) Directorate which had about 86 percent of the staff and 78 percent of the budget of the Department. While implementating the PBS, the management team realized that ownership of PBS was lacking from the Chief Directorate Health in Mpumalanga. One member of the management team pointed out that if the Directors, Chief Directors and MEC are not committed to fulfilling their responsibilities in terms of the PFMA, then the process will not proceed smoothly.

PBS had to be learned, and then taught, to over two hundred officials throughout the Department involved in budgeting and payments. This was important to the long-term viability of the PBS. Several workshops, and frequent training sessions, and visits to district management teams resulted in a capacitated workforce in the Directorate. The fundamental guide in the process has been the PFMA. Currently there is an understanding of what PBS means among managers involved in the budgeting process. The interviewees agreed on the understanding that PBS means you must have specific indicators that talk to the sector and clear mechanisms to achieve those indicators. Another interviewee stipulated that one must assign budgets appropriately to key objectives with monitoring to ensure achievement of results. One interviewee stipulated that one must budget according to the needs and expected outcomes for that particular financial year.

#### **4.10 Problems with the Previous Budgeting System in Mpumalanga**

Specific shortcomings raised by the interviewees were that the budget system was just a line-item system which concentrated only on inputs. There was no specification of outputs or outcomes, and therefore no way to measure performance. There was a lack of integration between planning and budgeting, in particular, budgeting was not informed by the strategic planning of the Chief Directorate: Health. Although management had done a great deal of strategic thinking, there was no clear mechanism for translating this into action throughout

the Chief Directorate. The budget was merely an increase on the previous year's figures.

The interviewees further mentioned that there was no procedure for priority setting, and no way to channel funds to priority programmes. There was never any attempt to match budget to outputs. The interviewee stated that National and Provincial priorities were not available to the public. There was no transparency in terms of budget allocations. No one knew what to expect from the provinces. The interviewee further stated that previously, the budget was based on increases without knowing the outputs and outcomes. The budget was finance driven rather than service delivery driven. There was also an inability to link budgets to key government policy objectives. Another interviewee stated that there was no consultation with other stakeholders. Budgeting was done without looking into the needs of the department.

There was no correlation between clients' needs and the budgeting process. In terms of operational processes, there was no provision of management information. There were no detailed reporting procedures, which made it difficult to determine the impact of expenditure. There was no sense of responsibility for managing expenditure. The lines of responsibility and accountability were unclear, which made it easy to shift the blame. Moreover, without capturing outputs and linking the inputs with outputs, it was difficult for health service officials to conceptualise what the funds were there for, and what their responsibilities were in relation to those funds. There was no clear understanding of the budgeting system within the Directorate (Shall, 2005: 47-48).

Shall (2005) argues that in terms of management, there was essentially no link between health sector management and financial management and budgeting. There was no connection between the way money was managed and the objectives of the Chief Directorate: Health. On the other hand there was no appreciation on the finance side of the need to support service delivery. The organizational and management structures, as well as the lines of responsibility, did not allow for proficient financial management.

Shall (2005) further argues that in terms of the budget structure, line functions were confused with management functions. As a result, management was more concerned with intervening in line functions, than focusing on strategic planning, monitoring and evaluation. The structure was economically irrational in that functions such as laundry were centralized at the provincial level rather than being decentralized to each hospital.

The problems discussed above prompted a fundamental restructuring of the budgeting system used by the Chief Directorate: Health in Mpumalanga. The Chief Directorate had at the time undertaken to implement the policy guidelines set out by the National Department of Health which included:

- Decentralization of services to the regions and districts to bring the services close to the people;
- Adoption of the district health system as the vehicle for health care delivery in the province;
- The choice of primary health care as the strategy for the delivery of universal health care to individuals, families and communities in the province;
- The need to involve stakeholders in planning and delivery of health services to the communities through meaningful community participation; and
- The need and desire to create a health service that cares for all and is responsive to clients needs.

In order to comply with the above policy guidelines, the Chief Directorate: Health had to adopt the following broad policies, priorities and strategic goals:

#### **4.11 Broad policies, priorities and strategic goals of the Department**

- Addressing communicable disease including HIV/AIDS, TB and Childhood illness such as pneumonia and other related diseases;
- Developing human resources: the department has committed itself to putting into place mechanisms to attract and retain scarce skills overall;

- Infrastructure component: this is in support of the hospital revatalisation programme;
- Strengthen the primary health care services as well the development of the District Health System by ensuring funding shifts to PHC services;
- Provision of developmental social welfare services to children, older persons, people with disabilities, and children; and
- Train, educate, re-deploy and employ a new category of workers in social development (Strategic Plan, 2005/06: 16).

The above policy priorities act as the drive for the Department to fulfill its goals of service delivery within the Province of Mpumalanga. It is for this reason that the Chief Directorate: Health in Mpumalanga decided to adopt performance budgeting system as a tool that will facilitate service delivery within the province. The decision to adopt the performance budgeting system arose primarily out of the district restructuring process. There was no budgeting structure or system in place for the districts and it was recognized that a new approach to health management, planning and budgeting was necessary. The District Health Systems Directorate thus took up the challenge of introducing a new system which would totally change the budgeting, financial planning and management systems for the districts (Shall, 2005).

#### **4.12 Link between research questions and findings of the study**

##### **4.12.1 Who is responsible for implementing performance-based budgeting and specifically, operationalising measures?**

As expected, numerous problematic issues arose once the implementation process had begun. These have been grouped into the categories of political, administrative and technical issues.

##### **(i) Political Issues**

Shall (2005) points out that the political issues that arose during the implementation process related to the coherence and consistency of the process, the acceptability of the new system, and the quality of leadership. Each of these is discussed in turn.

## **(ii) Coherency and Consistency**

The implementation of the system was not conceptualized thoroughly enough. The Chief Directorate: Health did not know exactly what was expected in the implementation of the new system. A detailed project implementation plan should have been developed, with both the consultants and the Chief Directorate providing input. It would also have helped, in this regard, to have had a situational analysis performed for the Chief Directorate: Health to determine exactly what existed in terms of capacity, infrastructure and existing systems (Shall, 2005: 30). One interviewee mentioned that currently there is an understanding of what needs to be done although the issue of capacity is still the problem at the managerial level.

## **(iii) Political Acceptability**

Officials in the Chief Directorate: Health were initially hesitant to adopt a new system because national systems had not changed. Provinces with weak management capacity are less willing to adopt systems that are not driven from the top. They cannot cope with the existing situation, and they are therefore less likely to adopt a new system which is a major challenge. However, Folscher and Cole (2004) emphasized that political involvement in budgeting is important. They argue that the mechanisms of the budget process should ensure that the role of political decision-makers is constructive and contributes to more effective spending. A continuous role for Cabinet, stitched in the budget process, is a critical feature of the reformed process in South Africa. Folscher and Cole argue that transparency of budget process is another important element of political acceptability.

One interviewee mentioned that when performance budgeting was introduced there was a lack of political acceptability. There was a sense of reluctance mainly due to

the introduction of the new system. As already mentioned by Shall (2005) provinces with weak management capacity are less willing to adopt new systems.

#### **(iv) Quality of Leadership**

There was a serious lack of management capacity at particular management levels in the Chief Directorate: Health. Managers appeared unable to make decisions, and were unwilling to be held accountable for any decisions made. Managers were not pro-active. There was no culture of management. Instead the focus was on administration (Shall, 2005: 32). Another interviewee mentioned that one still finds the same situation in the current management. “No one wants to be held accountable for decisions made”. The lack of management capacity at management levels is still a problem in the Directorate. In order to implement performance budgeting there is a need for a serious intervention on the issue of skills within management.

One of the interviewees stated that quality information, information officers and skills information officers are needed to effectively implement performance budgeting within the Department. Another interviewee stated that the implementation process of performance budgeting is linked to the strategic plan objectives of the Department but the main problem is reaching consensus regarding key objectives. One interviewee mentioned that, “though we are using performance base budgeting we are still expected to have spent 50% of the budget by September and one’s annual plan is not taken into consideration. Allocation is still affected by the previous year expenditure rather than the activities of the current year”.

For effective implementation of performance budgeting within the Department, interviewees suggested the following:

- Department should realize that there is a need for additional funds, capable programme managers and capable human resource at all levels;
- Intergovernmental relations are crucial in addressing performance budgeting obstacles within the Department;

- Adequate financial capacity is needed for the planning as well as monitoring process;

#### **4.12.2 Has performance budgeting begun to improve service delivery within the Department of Health in Mpumalanga?**

When asked about the impact of performance budgeting in improving service delivery, the interviewees mentioned that performance budgeting gives programme managers an opportunity to position themselves strategically to improve service delivery. They felt that performance budgeting should improve service delivery as resources are correctly focused on priority areas. One interviewee mentioned that performance budgeting might assist in spike spending on the last quarter of the financial year since monitoring is on quarterly basis and is according to the annual plan. This is because the emphasis is on activities budgeted for rather than just rands and cents.

The interviewees had different views on whether performance budgeting has really improved service delivery of the Department. One interviewee mentioned that previously the Department had been recording very high under-spending. Since the implementation of performance budgeting, the Department has moved from that status quo on both on equitable shares and grants. “As a sector we are yet to link increased expenditure to improved service delivery. It takes time to measure impact. Outputs are measurable, annual reports are helpful in this regard”. One also needs to consider the importance of inputs in this budget process. According to IDASA (2004) the cost of inputs must not exceed the budgeted amount. Efficiency is about how government works with inputs in relation to outputs. IDASA (2004) research further highlights that a budget is managed efficiently when inputs are used in a way that produces the most possible outputs. A budget is managed effectively when spending brings about the outcomes it sets to achieve.

On the other hand, some interviewees felt that service delivery had not improved as expected. They argue that this is due to the lack of financial support to line managers. The respondents felt that there is still a need for training on financial

management. Programme managers interviewed agreed that the Department is in line with key budget reform initiatives.

#### **4.12.3 Why is it important to link performance budgeting with policy priorities of government?**

Respondents were asked about the importance of linking budgetary allocations with the policy priorities. An interviewee stated that policy priorities are informed by the needs of people. Linking budgetary allocations with policy priorities is the same as linking spending with the needs of the people. Treasury Regulations (2006) stipulate that objectives that are set out in the strategic plan require solid linkages between planning and budgeting. The respondents felt that the Department is still struggling to align policy priorities with budgeting. The strategic plans are there but implementing those priorities according to plan is still a challenge. The interviewee further mentioned that policies are priorities of the Department and they need to be budgeted for as a priority. This allows the country to move in the same direction and makes it easy to monitor and evaluate the performance of each province. Folscher and Cole (2004) noticed that within budgeting systems, budget planning on its own is not sufficient – it must be accompanied by systems that ensure disciplined use of resources and improved incentives for delivery. The respondents mentioned that the incentives for delivery are lacking. The understanding of what needs to be done with regard to performance budgeting is there but incentives for action are the impediments to service delivery.

#### **4.12.4 What oversight capacity is provided by the legislature in South Africa?**

The main legislatures that play the oversight role are the PFMA and Treasury Regulations. There is an understanding within the public servants involved in budgeting of what they are expected to do. Although there is an understanding implementation is still problematic. Programme managers are not transparent enough and this makes it difficult to assess the effectiveness of the current legislation in South Africa.



#### **4.12.5 How can accountability be improved when applying performance budgeting?**

Accountability can be improved through law enforcement within government departments. The provincial departments are still faced with unqualified audit reports because of the lack of accountability by programme managers. The Mpumalanga Department of Health and Social Services is faced with the same problem of lack of accountability. This affects its performance and this makes performance budgeting to be not effective enough in terms of improving service delivery within the province.

#### **4.13 Chapter Summary**

As an attempt to ensure service delivery the Department of Health in Mpumalanga ensured that activities are in line with the strategic goals of the department. Previously, before implementation of performance budgeting, the budget system was just a line-item system which concentrated only on inputs. In terms of management, there was essentially no link between health sector management and budgeting. The interviewees agreed that there has been an improvement in terms of service delivery within the Department since performance budgeting gives programme managers an opportunity to position themselves strategically to improve service delivery. Some respondents felt that performance budgeting should improve service delivery as resources are correctly focused on priority areas. Previously, before the implementation of performance budgeting, the Department has been recording very high under-spending. However, the Department has moved from this status quo on both equitable shares and grants.

The link between policy priorities and budget allocations has been identified as the key part of this Chapter. Linking budgetary allocations with policy priorities is the same as linking spending with the needs of the people. The respondents agreed that there is a link between policy priorities and budgeting within the Department but felt that there are still challenges in getting this right. Policies are priorities of the Department. Therefore, they need to be budgeted for as a priority. The respondents mentioned that the incentives for delivery are lacking. The understanding of what

needs to be done with regard to performance budgeting is there but incentives for action are the impediments to service delivery.

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## CHAPTER 5

### 5.1 Conclusion

According to the research findings of this thesis, budget reform has some positive and negatives outcomes. The positive outcomes are:

- Performance budgeting is playing a crucial role in improving service delivery within the Department of Health and Social Services in Mpumalanga;
- There is greater understanding of how performance budgeting works within the Department;
- There is a strong emphasis on performance and accountability within managers;
- The Department is putting greater emphasis on strategic planning and financial management. Both these are crucial when applying performance budgeting;
- The Department of Health and Social Services is more focused on delivery outcomes.

On the other hand, there are some negative outcomes of performance budgeting. The negatives are as follows:

- Politicians and managers involved in the budgeting process do not want to be held accountable for their actions. They tend to ignore some functions and this is affecting service delivery within the province;
- Application of performance budgeting needs to be done in a good enabling environment meaning good managerial level. As it stands in Mpumalanga Department of Health and Social Services, there is a huge shortage of managerial capacity. As a result performance budgeting is not delivering as it is expected.

The thesis also discovered that within the Department of Health and Social Services managers are still struggling to link policy priorities with budgeting. This is affecting service delivery within the province.

## 5.2 Recommendations

It was clear from the findings that the link between performance budgeting and policy priorities remains a challenge for the Health Department in Mpumalanga. Although strategic plans are in place successful implementation of these plans is lacking. This affects service delivery within the Province. For successful implementation of performance budgeting within the Department, the following must happen:

- The successful implementation of performance budgeting requires change at both the political and managerial level. It is important that the system is acceptable to political structures, and that good quality leadership exists;
- It is important to educate and familiarize top management with performance budgeting system for successful implementation of the system;
- Co-ordination between strategic planning, resource allocation and policy analysis is required to prevent any obstacles in implementing the system;
- Outputs and outcomes must be specified in advance and the outputs must be measurable;
- Most importantly, the department should focus more on managerial capacity for successful implementation of the system in Mpumalanga Department of Health.

For successful implementation of performance budgeting in Mpumalanga the department should consider the following steps suggested by Diamond (2001):

- Keep participants focused on objectives, publicizing these objectives is one approach to create incentives and put pressure on participants to meet these objectives, and enforcing efforts to hold them accountable for achieving these objectives;
- Rewarding good performance and sanctioning poor performance. Establishing clear performance accountability involves first a threshold level of basic financial and personnel management systems to be in place to report on performance and second a performance orientated from linking rewards to performance;

- Greater application of information technology. Improved classification systems to identify programmes, so that costs can be allocated to individual activities, to be composed with the outputs of these activities;
- Moving performance indicators from quantity to quality. The importance of performance indicators has long been recognized in reforms associated with performance budgeting.

(Diamond, 2001: 18).

In order to improve service delivery in the Health Department, there must be greater policy focus and prioritization in resource allocation, programme planning and management. Stronger motivation on the part of line managers and service providers is very important.

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